198593

LAW OFFICES

JOHN H. BROADLEY & ASSOCIATES, P.C.

CANAL SQUARE
1054 THIRTY-FIRST STREET, N.W.
WASHINGTON, D.C.
20007

(202) 333-6025
(202) 333-5685 FAX

INTERNET
JBROADLEY@ALUM.MIT.EDU

May 16, 2000

JOHN H. BROADLEY

Honorable Vernon Williams
Secretary
Surface Transportation Board
1925 K Street NW
Washington, D.C. 20423-0001

ENTERED
Office of the Secretary

MAY 16 2000

Part of
Public Record

Re: Ex Parte 582 (Sub-No.1), Major Rail Consolidation Procedures

Dear Mr Williams:

Enclosed for filing in the captioned proceeding is an original and 25 copies of the COMMENTS OF THE PORT OF SEATTLE, THE PORT OF TACOMA AND THE PORT OF EVERETT REGARDING THE BOARD'S FUTURE MERGER GUIDELINES. Also enclosed is a 3.5" disk containing the text of the filing in WordPerfect 9 format.

I have also enclosed an extra copy of comments which I ask that you date stamp and return with our messenger.

I have caused copies of these comments to be served on all parties listed on the Board's service list served on April 28, 2000 as modified by the Board's decision served on May 12, 2000 by depositing copies in the United States mails, postage pre-paid, addressed to counsel for the parties.

Yours very truly,

John Broadley

John Broadley

Enclosures

BEFORE THE
SURFACE TRANSPORTATION BOARD
Washington, D.C.

RECEIVED
MAY 16 2000
MAIL MANAGEMENT
STB

MAJOR RAIL CONSOLIDATION PROCEDURES	)	Ex Parte No. 582 (Sub-No. 1)

ENTERED
Office of the Secretary
MAY 16 2000
Part of
Public Record

COMMENTS OF THE PORT OF SEATTLE, THE PORT OF TACOMA AND THE PORT OF EVERETT REGARDING THE BOARD'S FUTURE MERGER GUIDELINES

The following comments and proposed guidelines are submitted jointly by the Port of Seattle, the Port of Tacoma and the Port of Everett (collectively, "the Ports"), acting by their undersigned Officers, pursuant to the Surface Transportation Board's Advance Notice of Proposed Rule Making in this proceeding served on March 31, 2000.

THE PORTS OF SEATTLE, TACOMA AND EVERETT

The Ports of Seattle and Tacoma need no introduction to the Board. Together these ports handle approximately 3 million TEUs per year, a number roughly equal to all the number handled by the Port of New York, and second on the West Coast only to the ports of Los Angeles and Long Beach. Approximately 75% of the trans-Pacific containers handled by the Ports move out of the Pacific Northwest region to other parts of the country, primarily to or through the Chicago gateway. Rail service is an indispensable part of the business of the Ports Without adequate rail service between the Pacific Northwest and other parts of the country, the Ports will lose their ability to compete for import and export container business between the United States and other Pacific Rim countries. The Port of Everett currently operates eight berths on 100 acres of land and handles approximately 1 million tons of cargo per year. The principal exports are logs, lumber, and fresh and frozen agricultural products and the principal imports are bulk alumina ore and specialized aircraft parts for Boeing. The port depends on rail service provided by Burlington Northern Santa Fe.

The Ports are municipal corporations organized under Washington law. The Port of Seattle is located in King County, the Port of Tacoma is located in Pierce County, and the Port of Everett is located in Snohomish County. Each port is managed by elected Port Commissioners and an Executive Director. The investment in marine facilities at each port reflects the large volume of container traffic that flows through the ports of Seattle and Tacoma and the general cargoes that move through the Port of Everett. In the case of the Port of Seattle, the 1998 combined investment in marine facilities was over $1 billion with an annual capital expenditure of $135 million. In the case of the Port of Tacoma, the 1999 combined investment in marine facilities was approximately $400 million with an annual capital expenditure of $55 million. In the case of the Port of Everett the 1998 combined investment in marine facilities was approximately $77 million with an annual capital expenditure of approximately $15 million.

Attachment No. 1 is the 1998 Annual Report of the Port of Seattle. Attachment No. 2 the 1999 Annual Report of the Port of Tacoma. Attachment No. 3 is the 1998 Annual Report of the Port of Everett.

OVERVIEW OF THE ISSUE

Since 1920 federal policy has been to encourage the consolidation of railroads in the expectation that rail service provided by fewer railroads with fewer interchanges would be more efficient and higher quality rail service. The original view of Congress was that the consolidation process should be planned and implemented by the Interstate Commerce Commission itself. *See* Sections 5(4) - 5(8) of the Interstate Commerce Act added by the Transportation Act of 1920, February 28, 1920, c.91, sec. 407, 41 Stat.481. In the late 1930's Congress recognized that Commission planned and initiated transactions were not occurring and changed the approach in the Transportation Act of 1940. Under the revised approach, consolidation transactions were to be initiated by the railroads and the role of the Commission was to ensure that the proposed transactions were in the public interest as measured by factors specified by Congress and assessed by the Commission. Congress gave the Commission broad conditioning power to ensure that the transaction as implemented furthered the public interest. *See* Section 5(2) of the Interstate Commerce Act as amended by the Transportation Act of 1940, September 18, 1940, c.722, sec.7, 54 Stat. 905.

As a result of the collapse of a large part of the railroad industry in the late 1960's and early 1970's and the weak financial condition of much of the remainder, the Commission took more aggressive steps to encourage and facilitate consolidations that would eliminate excess capacity and reduce redundant facilities while still protecting vital public interests. The result was the Commission's merger guidelines that are now in place at 49 CFR 1180.1. Those guidelines focus on protecting the public from a direct and significant reduction of competition and from the loss of essential services as a result of a transaction crippling a carrier providing them. *See* 49 CFR 1180.1(c)(2)(i) and (ii); and *Lamoille Valley RR. v. I.C.C.*, 711 F.2d 295 (D.C. Cir. 1983). The Commission specifically rejected using its conditioning power to reshape transactions, recognizing that such restructuring might so reduce the value of the merger to the carriers that it would not be consummated. Such a failure would mean a loss of benefit to the public, or that the cost of such modifications in terms of merger benefits and efficiencies would exceed the public benefits of the enhanced conditions. *See Union Pacific -- Control -- Missouri Pacific; Western Pacific*, 366 I.C.C. 462, 562-65 (1982).

We have now reached the point in rail mergers in the United States where there appears to be only one further possible round. The nation's rail system now consists of two large carriers operating primarily west of the Mississippi River and two large carriers operating primarily east of the Mississippi. In addition, there are two Canadian carriers, one of which is transcontinental and also operates lines in the United States reaching Detroit, Chicago, New Orleans, Dallas and Jackson, and the other which is almost transcontinental (terminating in Montreal) and operating lines in the United States between Winnipeg and Chicago, reaching Chicago from the east through arrangements with other railroads, and operating lines between Niagara Falls/Buffalo, NY and Montreal on the one hand and New York City and several other mid-Atlantic destinations, including Philadelphia, on the other. In addition, there is a modest size class I railroad that operates between Kansas City and the Gulf Coast, and a number of regional railroads that operate in New England, Florida, Wisconsin and Minnesota, and Montana.

The final round of major mergers is likely to lead to the creation of two major carriers in the United States through the merger of one of the western carriers with one of eastern carriers. The other participants in the North American railroad business will likely align themselves in one way or another with one of the two continent-wide mega-carriers. **The overarching issue in this final round of mergers will be whether the resulting rail system will meet the needs of the public for efficiency and competition.** The reason this issue is overarching is that once this final round of mergers is consummated, the Board will not have an opportunity to change the situation under present legislative and regulatory arrangements. The Board's powers to restructure the rail industry to promote competition in the absence of mergers is severely limited under current law and regulations. The key problem for the Board is to ensure that this final round of mergers will create carriers structured in such a manner that the nation can live with the resulting system and that it will serve the public interest in an environment where reduction of redundant capacity is not the central issue. It must be emphasized that the Board faces no urgent need to encourage mergers to reduce excess capacity as the excess capacity and redundant facilities in the system now have been eliminated. Indeed, the experience of the past several years is that capacity in the rail industry is severely constrained either as a result of insufficient investment or inefficient use of existing facilities.

These comments will address the two central issues that will face the Board in the final round of mergers. First, what structure of the rail industry is in the public interest in the long term? Second, what merger guidelines should be established to ensure that future mergers promote that structure?

A RAIL INDUSTRY STRUCTURE THAT SERVES THE PUBLIC INTEREST

It has been said that the fundamental problem with railroads is that if they fail to supply service to the shipper's[1] satisfaction, the shipper usually can not pick up the telephone and call another railroad. The Board's objective in this final round of rail mergers must be to ensure that

[1] We will use the term "shipper" in these comments to refer to both classic shippers and receivers, and also intermediate transportation service providers such as ports.

shippers have the option of picking up the telephone and calling another railroad where this is practicable. This minimum level of rail-to-rail competition is the only long-term assurance (i) that the railroads will receive appropriate market signals, (ii) that the railroads will aggressively pursue service enhancements and cost reductions, and, most fundamentally (iii) that railroads will respond promptly and efficiently to changing economic and social conditions. Railroads facing rail-to-rail competition will begin to act more like other businesses in the US economy focusing on solving problems for their customers and making every effort to deal with complications and impediments as they arise, at the lowest possible cost. They will do this out of pure economic self-interest -- to ensure that the shipper does exercise his option of picking up the telephone and calling another railroad.

The Ports believe that such a competitive structure of the rail industry will provide far better solutions to both current and future problems than can be provided by dead-hand protective conditions imposed in mergers that take place under what may be radically different economic and social circumstances than the shippers, the Ports and the railroads will face in the future. Moreover, the Ports do not believe that an industry structure where they as Ports may have competitive rail service, but large numbers of other shippers in the economy do not, is a satisfactory structure. The issue is not simply the existence of rail-to-rail competition for the Ports' traffic, but the existence of a type of railroad industry that will respond to the challenges and opportunities of an ever changing market. This type of rail industry will only develop when railroads generally have to operate in a pervasively competitive market facing real rail-to-rail competition. For the long term, the effects of pervasive rail-to-rail competition on the nature of railroads is more important than simply ensuring that today a limited number of favored shippers have competitive rail options.

The long-term evolution of the structure for the rail industry that is contemplated in these Comments is not radical or novel. To the contrary, it is structure that most American industry has had since the beginning, a structure that is vigorously maintained through application of the antitrust laws.[2] Nor is such a long-term structure radical or novel in network industries. In the telephone industry AT&T's network was first opened to long distance competitors in the late 1970's, was substantially restructured to support long distance competition on a level playing field in 1984, and is now in the process of moving to competition in the local service market under the auspices of the Telecommunications Act of 1996. *See,* e.g. *MCI v. AT&T,* 709 F.2d 1081 (7th Cir.), *cert. denied* sub nom. *AT&T v. MCI,* 464 U.S. 891 (1983); *United States v. AT&T,* 552 F.Supp. 131 (D.DC 1982), *aff'd* 460 U.S. 1001 (1983); *Telecommunications Act of 1996,* P.L. 104-104, February 8, 1996, 110 Stat. 56. The natural gas industry was transformed from a series of regulated monopolies from well-head to burner tip largely by the use of FERC's existing powers, *see* e.g.

---

[2] The Ports themselves are acutely aware of competition for port services. The Ports face competition for trans-Pacific container traffic from the Port of Vancouver, BC, the Port of Oakland, CA, and the Ports of Los Angeles and Long Beach, CA. Moreover, for trans-Pacific container traffic, the Port of Seattle and the Port of Tacoma are themselves in vigorous competition. Furthermore, the Port of Everett has recently announced its intent to enter into trans-Pacific container trade which will create further local competition.

Order No. 636, *Pipeline Service Obligations*, III FERC Stats. & Regs. (CCH) p. 30,939 (April 8, 1992), Order No. 636-B, *Denying Rehearing and Clarifying Order Nos. 636 and 636-A*, 61 FERC p. 61,272 (November 27, 1992), with the result that natural gas pipelines now operate in an increasingly competitive gas transportation market. This has been backed in many states by legislation permitting competition in the local market with the result that not only large industrial consumers have competitive gas purchase options but also retail users. Similarly, the electric power industry has been undergoing a transition to a more competitive structure with the separation of the potentially competitive generating market from the monopolistic aspects of the system -- transmission and local distribution. *See* e.g. Order No. 888, *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities*, 61 F.R. 21540 (1996), 76 FERC 61,009 (1996), 76 FERC 61347 (1996), 79 FERC 61,182 (1997), 82 FERC 61046 (1[illegible] [illegible]tion for review pending *sub nom. Trans-Access Policy Study Group v. FERC*, D.C. Cir. [illegible], submitted November 3, 1999.

Indeed, in much of the rail industry itself, there is already substantial rail-to-rail competition. Shippers in many parts of the country have service from two rail carriers and the Interstate Commerce Commission at times sought to enhance that situation, perhaps most dramatically by insisting that there be two-carrier service in much of the Powder River Basin where approximately 1/3 of the nation's coal is produced and shipped almost exclusively by rail. *See Burlington Northern and Chicago North Western Transportation Co. -- Construction and Operation -- Between Gillette and Douglas in Campbell and Converse Counties, Wyoming*, 348 I.C.C. 388 (1976); and *Chicago and North Western Transportation Company -- Construction and Operation*, 363 I.C.C. 906 (1981). In the recent acquisition of Conrail by CSX and NS, shippers with annual rail expenditures of over $700 million that had been captive to Conrail are now in the Shared Assets Areas where they have direct access to both CSX and NS through the intermediary of a neutral terminal company. *See CSX Corporation et al. and Norfolk Southern Corporation et al. -- Control and Operating Leases/Agreements -- Conrail, Inc. et al.*, STB Finance Docket No. 33388, Decision No. 89 (Served July 23, 1998).[3] The Ports are proposing that further major mergers in the railroad industry be conditioned on the merging carriers providing to all shippers on the merging carriers the same option to "call another railroad" that many rail shippers already have, to the extent that such competition is practicable.

---

[3] At p. 129 of Decision No. 89 the Board stated unequivocally that:

> The most important public benefit resulting from the transaction will be a substantial increase in competition by allowing both CSX and NS to serve where only Conrail served before. This will bring new competition to shippers in such markets as Southern New Jersey/Philadelphia, Northern New Jersey, Detroit, Ashtabula and the Monongahela coal fields. Applicants estimate that $700 million worth of traffic per year will receive new two-carrier competition. . . .

The structure of the rail industry that results from the final round of mergers will likely prevail for some considerable period of time. It is imperative that in this final round of mergers the Board take the opportunity to exercise its very broad authority under existing law to ensure that the resulting railroad industry structure provides the amount and character of rail-to-rail competition that will place a continuing pressure on each railroad to provide attractive service and pricing packages to its customers and force the industry as a whole to respond to changing circumstances promptly and efficiently. In our view, the minimum level of rail-to-rail competition that emerges from this final round of mergers must satisfy two conditions.

The first condition, which we refer to as "Local Access," is that *within* areas where access to two carriers is practicable, all shippers have such access. The second condition, which we refer to as "Long-Haul Access," is that *between* major market areas there be at least two fully competitive rail routes served by competing long-haul carriers. We will discuss each of these conditions in greater detail.

Local Access[4]

A competitive rail market requires that shippers have access to at least two rail carriers. This means that there must be in place a practical and economic method by which they can "call another railroad" if they become dissatisfied with the price and service of the railroad with which they are dealing, even if the lines of only one railroad reach the shipper. The Ports have focused on how to provide local access within major market areas such as the complex along Puget Sound that includes Seattle, Tacoma and Everett because the largest number of shippers is located in such major market areas and because the Ports and their ultimate customers are located in such areas.[5]

Within major market areas there are four general approaches that can be used to ensure that all shippers have access to at least two railroads.

1. The CSXT/NS Shared Assets Concept.

The first general approach to providing local access is that proposed and implemented by CSXT and Norfolk Southern in the shared assets areas they established when they broke up

---

[4] These proposed guidelines do not contemplate a reciprocal arrangement for local competition. However, the Board may wish to consider whether including such an arrangement using its other powers under the Act may be in the public interest.

[5] The Ports recognize that certain major rail shippers are not located in major market areas. While, as a general principle, they believe that the same competitive options should be available to such shippers, they recognize that the choice of competitive alternatives may present different issues than in the major market areas and therefore do not express any view on the competitive alternatives which could be used in such cases.

Conrail. In northern New Jersey, southern New Jersey and the Detroit area, the shippers on the former Conrail lines have direct access to both CSXT and NS through switching service provided by a terminal railroad (still called "Conrail"). The terminal railroad performs all the local distribution and collection of traffic while the line-haul carriers deliver and pick-up fully assembled trains at the yards in the shared assets areas.

2. The Canadian Interswitching Concept.

The second general approach is that applied in Canada where shippers and receivers served by only one carrier but located within 30 kilometers (approximately 20 miles) of an interchange with a competing carrier have the right to receive cost-based switching by their serving carrier to the interchange. The Canadian Transportation Agency calculates the costs and sets switching rates based on those costs which vary by mileage bands and by number of cars being switched. In unusual cases, the Canadian Transportation Agency can order switching service to a shipper outside the 30 kilometer radius. A copy of the Canadian legislation (Sections 127 and 128 of the Canada Transportation Act of 1996) and regulations implementing it (Canadian Transportation Agency Regulations Respecting The Interswitching of Rail Traffic) are attached hereto as Attachment No. 4.

3. Trackage Rights.

The third general approach is that contemplated by 49 U.S.C. 11102(a) whereby one railroad can obtain trackage rights over another railroad to permit it to access a shipper or group of shippers in a terminal area.

4. Shortlines.

The fourth general approach is to provide access through a shortline railroad. A shortline can be viewed as a small shared assets area. In many cases a shipper located on a shortline has access to two or more carriers from the shortline. In some cases, however, the shipper's access to a second carrier is limited or precluded by so-called "paper barriers" established in the transaction that created the shortline. In other cases, the shortline physically connects only with one line-haul carrier. To the extent that the short line has physical access to two or more long-haul carriers, the elimination of paper barriers would provide the necessary local access. Where the shortline does not have physical access to a second long-haul carrier, its shippers can gain such access if the shortline is granted trackage rights over the existing connecting carrier to an interchange with a competing long-haul carrier.

Long-Haul Access

Shipper access within a major market area to two competitive rail carriers is a necessary but not a sufficient condition for effective rail-to-rail competition. In order for rail-to-rail competition to be fully effective, the two competitive carriers to which shippers have access need to be, or to have access to, two competing line-haul carriers with roughly equivalent routes between major market areas. There is no cookbook list of conditions necessary or sufficient for rough equivalence of raii routes. There are a number of factors that should be taken into account such as:

(i) Comparative length of each route
(ii) Comparative ruling grades on each route
(iii) Line capacity on each route
(iv) Ownership versus trackage rights
(v) Potential for capacity expansion
(vi) Other factors affecting cost of service and quality of service.

In many cases major market areas already will be connected by competing routes served by long-haul carriers that are roughly equivalent. Where this is not the case, however, the final round of mergers must be conditioned on the merging carriers taking steps to correct this condition where it is within their capacity to do so. For example, where the long-haul competitor of a merging carrier has an inferior route into a major market area, corrective steps could including reversing the landlord -- tenant relationship with respect to a line in order to provide both carriers access to a market on owned trackage, exchange of lines, or, where multiple routes are not feasible or are not economically warranted, joint ownership of lines with use by both carriers on equal terms.

MERGER GUIDELINES TO FURTHER THE PUBLIC INTEREST

The following discussion and proposed guidelines are designed to provide a framework that would lead to the imposition of conditions on transactions involving two or more Class I railroads that will move the railroad industry toward a more competitive structure if such mergers are proposed and implemented. Several points should be kept in mind regarding this proposal:

First: No Board Initiative. This is not a proposal that the Board take the initiative in restructuring the industry. The proposed guidelines will have no effect on the industry structure in the absence of merger activity involving two or more Class I railroads. The guidelines will simply assure that if such merger activity takes place, the merged carriers will face customers who have more competitive options than is the case today.

Second: No General Restructuring. This is not a proposal that a merger of two Class I railroads should precipitate a general restructuring of the industry. Carriers that are not applicants in the merger proceeding will not be required to provide shippers on their lines with access, though they will benefit from access to shippers on the lines of the merging carriers. It should be repeated: *Non-applicants and shippers located on their lines will not be affected directly by the proposed guidelines.* This is not to say that there might not be indirect effects on non-applicant carriers. The non-applicant railroad will have the opportunity to compete for traffic on the merged carriers as a result of the access conditions. On the other hand, shippers making plant location decisions may be encouraged to place new facilities on lines where there is better access to the detriment of non-applicant carriers.[6]

Third: A Fail-Safe Proposal. There is some dispute in the railroad community regarding the fundamental economics of the railroad industry -- or at least the part of the business that relates to the supply of infrastructure services. It has been contended that at least some part of the railroad business may be a natural monopoly -- that the marginal costs of supplying infrastructure services declines over all relevant volumes -- and consequently that railroads need captive shippers from which they can recover their fixed costs.[7] If this is the case, Class I railroads will not merge under these guidelines because the price of such a merger will be the loss of all (or substantially all) of the merging carriers' captive shippers. On the other hand, if the merger benefits are substantial, they may well exceed any losses arising from granting access to shippers. The key point is that this will be a decision to be made by Class I rail carriers contemplating a merger.

1. Scope of the Guidelines.

The concerns that we address relate to the final major restructuring of the North American rail system. They do not related to transactions that do not involve at least two Class I carriers, nor do they apply to transactions involving two or more Class I carriers that do not result in a substantial change in the relationship between the two carriers. Thus, the revisions to the merger guidelines proposed below apply only to transactions that involve two or more Class I carriers and that involve the acquisition or change control over rail assets having a fair market value exceeding $100 million, through acquisition or exchange of stock, or through lease, purchase, merger or any other transaction which is subject to the Board's jurisdiction. With respect to such transactions the proposed guidelines are a supplement to those already in place.

Proposed Guideline:

---

[6] These proposed guidelines do not contemplate a reciprocal arrangement for local competition. However, the Board may wish to consider whether including such an arrangement using its other powers under the Act may be in the public interest.

[7] *See* e.g. the discussion in *Ex Parte 347 (Sub-No. 1), Coal Rate Guidelines -- Nationwide*, 1 ICC2d 520, 526 (1985). *Compare* the discussion in *Finance Docket No. 32467, National Railroad Passenger Corporation -- Application Under Section 402(a) -- Consolidated Rail Corporation*, 10 I.C.C.2d 863 (1996) where the Commission stated:

> We will adopt the WSAC model here. As discussed below, that model recognizes that there are "economies of density" n24 below certain threshold tonnages, but that above those thresholds, there are no economies of density -- instead, damage to track and other rail property associated with MOW costs rises linearly with tonnages. n25

These supplementary guidelines apply to transactions subject to the jurisdiction of the Board under 49 U.S.C. 11323 that involve two or more Class I carriers and that result in the acquisition or change of control over rail assets having a fair market value exceeding $100 million. To the extent these supplementary guidelines are inconsistent with existing guidelines, the supplementary guidelines shall govern.

2. Policy of the Guidelines.

The overarching policy of the Board in approving a transaction covered by the supplementary guidelines should be to move the structure of the railroad industry substantially in the direction outlined in the discussion above. In furtherance of that policy, the Board should adopt a requirement that it will not approve a transaction subject to the supplementary guidelines involving two or more Class I carriers unless two conditions are satisfied. The first condition relates to the local structure of the industry and promotes shipper access to local carriers -- the ability of the shipper to "call another railroad." The second condition relates to the national structure of the industry and promotes fully competitive routes between major market areas in the United States. The two conditions are more fully described as follows:

Local Structure/Local Competition:[8]

(i) In each Competitive Market Area each shipper served by a Class I carrier involved in the transaction shall have access to a Competitive Carrier either through service by a neutral terminal or shortline railroad, by cost-based switching provided by the serving Class I carrier, or by trackage rights available to a Competitive Carrier at cost-based rates. The term Competitive Market Area means every point on each of the Class I carriers involved in the transaction that is within 20 miles of an interchange with a Competitive Carrier, or such greater distance as the Board might specify in specific cases. The term Competitive Carrier means a carrier that, either directly or through connections not involving one of the Class I carriers involved in the transaction, has access to substantially all Major Market Areas served by the Class I carriers involved in the transaction.

(ii) Each Class I carrier involved in the transaction shall eliminate all Paper Barriers with short line or regional carriers to which it is a party. The term Paper Barriers should be interpreted broadly to encompass all provisions of an agreement, direct or indirect, that restrain the ability of the short line or regional carrier to interchange with carriers other than the Class I carriers involved in the transaction.

---

[8] These proposed guidelines do not contemplate a reciprocal arrangement for local competition. However, the Board may wish to consider whether including such an arrangement using its other powers under the Act may be in the public interest.

(iii) Each Class I carrier involved in the transaction shall offer overhead trackage rights at cost-based rates to each shortline or regional railroad whose only physical connection with the national rail system is over a Class I carrier involved in the transaction. The trackage rights offer shall extend from the physical connection between the short line and the Class I carrier involved in the transaction to the nearest physical connection between the Class I carrier involved in the transaction and a Competitive Long-Haul carrier. Except as required by the Board in specific cases, such trackage rights need not be offered if the closest physical connection with a Competitive Long-Haul Carrier is more then 20 miles from the shortline's or regional railroad's connection with the Class I carrier involved in the transaction.

Long-Haul Structure/Long-Haul Competition:

(iv) Each Major Market Area served by a Class I carrier involved in the transaction shall have service by a Competitive Long-Haul Carrier. The term Competitive Long-Haul Carrier as used here means a carrier that, from the Major Market Area in question, has access to all other Major Market Areas either directly or through connections that do not involve use of the Class I carriers involved in the transaction. That access shall be substantially equivalent to that of the Class I carriers involved in the transaction. In applying this policy, the Board must interpret the terms -- Major Market Area, and Substantially Equivalent to further its new policy of moving the railroad industry to a new, more competitive structure.

Proposed Regulations:

It is the policy of the Board that any transaction subject to these supplementary guidelines shall, to the maximum extent possible, promote rail-to-rail competition within the United States and between the United States and adjacent foreign countries.

In furtherance of that policy, the Board will not approve any transaction subject to these supplementary guidelines unless, immediately following such transaction:

(a) Local Competition: each shipper in a Competitive Market Area served by one or more of the Class I carriers involved in the transaction shall have Direct Access to a Competitive Carrier.

(b) Long-Haul Competition: each Major Market Area served by one or more of the Class I carriers involved in the transaction shall be served by one or more Competitive Long-Haul Carriers; and

(c) Shortline Competition: each Class I Carrier involved in the transaction shall have:

(i) eliminated all Paper Barriers to which it is a party effective on the date of consummation of the transaction, and

(ii) offered to each Captive Short Line a trackage rights agreement at cost-based rates granting overhead trackage rights between the point of connection with the Captive Short Line and the nearest physical connection with a Competitive Line-Haul Carrier, provided, however, that if the length of trackage rights involved exceeds 20 miles, such offer need be made only if directed by the Board.

(d) Definitions: as used in these supplemental guidelines, the following terms shall have the meanings ascribed to them:

(i) Captive Short Line shall mean a Class III or Class II rail carrier whose only physical connection with the national rail network is through one or more of the Class I carriers involved in the transaction.

(ii) Competitive Market Area shall mean any point located on the lines of the Class I railroads involved in the transaction that is within 20 miles of an interchange with a Competitive Carrier, or such greater distance as the Board may prescribe in specific cases.

(iii) Competitive Carrier shall mean a rail carrier that either itself or through connecting carriers not affiliated with the Class I carriers involved in the transaction, reaches substantially all Major Market Areas reached by the Class I carriers involved in the transaction.

(iv) Competitive Long-Haul Carrier shall mean a rail carrier which, either directly or through connecting carriers not affiliated with the Class I carriers involved in the transaction, has access to each Major Market Area served by the Class I carriers involved in the transaction that is substantially equivalent to the access of the Class I carriers involved in the transaction. In determining

substantial equivalence, the Board will take into account (A) the length of the route, (B) the ruling grades on the route, (C) the ownership of the route, (D) the physical condition of the route, (E) the capacity of the route and the possibilities and cost of expansion, (F) the number and cost of interchanges involved, and (G) any other factors which bear upon the cost and quality of service over the route.

(v) Direct Access shall mean access through service provided by a neutral shortline or regional railroad or a neutral terminal company when applicable, otherwise the term shall mean (A) access through switching service provided by the serving carrier at a price that does not exceed the price that the Board would prescribe for switching service provided under 49 U.S.C. 11102(b), or (B) trackage rights provided at a price that does not exceed the price that the Board would prescribe for terminal trackage rights under 49 U.S.C. 11102(a). In the event that the shipper is not served by a shortline, regional railroad or a neutral terminal company, the choice of switching or trackage rights access shall be that of the serving carrier, unless the shipper can demonstrate that the serving carrier's choice does not provide effective rail-to-rail competition.

(vi) Major Market Area shall mean any Standard Metropolitan Statistical Area of the United States any comparable area in an adjacent foreign country, or any broader or narrower area designated by the Board in specific cases, in which the number of rail car originations plus rail car terminations exceeds 50,000 per year, or such smaller number as the Board may establish in specific cases.

(vii) Paper Barrier shall mean any provision of an agreement between a shortline or regional railroad and a Class I carrier involved in the transaction that either directly or indirectly constrains the ability of a shipper to route traffic over a carrier, other than the Class I carrier involved in the transaction.

3. International Aspects

North America is rapidly evolving into a single market, including a single transportation market. The Ports are acutely aware that they face competition from ports in Canada as well as from ports in the United States. The Board cannot ignore the fact that in the rail industry impediments imposed on the ability of railroads to compete outside the borders of the United States can have a clear and direct impact on the level of competition among rail carriers within the United States, and correspondingly on the quality and cost of rail service within the United States, including that provided to the Ports. Correspondingly, however, the Board cannot ignore the fact that its jurisdiction stops at the borders of the United States and that its conditioning power to change conditions outside the borders of the United States should be used neutrally and sensitively.

By neutral application of its conditioning power, we mean that the Board's conditioning power must be applied evenhandedly to require all carriers wishing to participate in the United States rail market to compete on a level playing field. If foreign companies wish to compete in the United States rail market they should be encouraged to do so and the Board should make clear that it will not use its conditioning power to discriminate against them. On the other hand, the Board should make clear that it will not tolerate a situation where a foreign carrier wishes to participate in the United States rail market into which the Board is seeking to insert additional competition, but seeks also to frustrate the Board's efforts in that regard by hiding behind its foreign status and favorable arrangements it might have in the foreign country.

By sensitive application of its conditioning power, we mean that the Board should attempt to shape its approach with respect to foreign activities affecting the United States rail market to be consistent with the requirements of foreign jurisdictions, where this can be done without undermining the Board's objectives for the United States rail market. Similarly, where conditions in the foreign market do not prejudice United States rail shippers or receivers or other railroads competing in the United States rail market, they need not be changed even where, if the conditions existed in the United States the Board's new policies would require a change. Put another way, it is not the Board's responsibility to promote the interests of foreign shippers, ports or railroads except insofar as that is necessary to provide a level playing field for rail-to-rail competition in the United States.

Two points of concern arise with respect to Canadian railroads seeking to operate in a competitive United States rail market.

First, with respect to local access, Canadian railroads cannot use their control over Canadian shippers shipping by rail to US destinations or over Canadian receivers receiving by rail from US origins to enhance their position in the US rail market. Fortunately, Sections 127 and 128 of the Canada Transportation Act requires railroads to provide switching access within 30 kilometers of an interchange with a competing carrier at cost-based rates specified by the Canadian Transportation Agency. Application of Sections 127 and 128 will provide substantially the same level of local access as contemplated for the United States and the Board's supplementary guidelines should reflect this.

Second, there is at least one Major Market Area in Canada where there is no long-haul competition -- the Port of Halifax which is served exclusively by Canadian National Railway. While service by a single railroad may disadvantage the Port of Halifax, it is questionable whether this condition would disadvantage US shippers or receivers or any railroad competing in the United States, provided that the shippers and receivers located on CN or CN controlled lines in the United States have access to Competitive Carriers and the Major Market Areas in which they are located have access to Competitive Long-Haul Carriers serving ports competing with the Port of Halifax.[9]

Proposed Regulations:

> *When these supplementary guidelines apply and one or more of the Class I carriers involved in the transaction has operations in a foreign country, or is affiliated with a company that has operations in a foreign country, the provisions of these supplemental guidelines shall apply to the operations of that company and its affiliate in the foreign country in the same manner as if those operations took place in the United States; provided, however, that*
>
> *(i) as used in these supplementary guidelines the term "foreign" shall mean only countries adjacent to the United States,*
>
> *(ii) with respect to rail operations in Canada, there shall be a rebuttable presumption that compliance with Sections 127 and 128 of the Canada Transportation Act of1996 constitutes the provision of Direct Access as required under these supplementary guidelines, and*
>
> *(iii) the Board may waive the imposition of a condition required by these supplementary guidelines to the extent it would have application in a foreign country where it has been demonstrated that the condition is not necessary to protect shippers or receivers in the United States or rail-to-rail competition in the United States rail market.*

---

[9] Without Local Access (access to Competitive Carriers) and Long-Haul Access (access to Competitive Long-Haul Carriers) CN would have the ability to focus its captive customers to the Port of Halifax. Shipper access to Competitive Long-Haul Carriers ensures that Halifax will be used only if the price and service package provided through that port are preferable to those provided by Competitive Long-Haul Carriers through other ports. Under these proposed supplementary guidelines, CN will have no coercive power over any shippers located on its lines within Competitive Market Areas to use the Port of Halifax.

4. Implementation of transactions

The implementation phase of several recent rail mergers has not been a happy experience for the railroads involved in the transaction, other railroads, shippers, or the Board. Unfortunately, once a transaction has been consummated and implementation problems have arisen, as a practical matter only the railroads involved can solve the problems. At that stage the Board's ability is limited, at best, to moving the pain and disruption around. Where there is a general service failure, a Board direction that shipper A be fully protected is likely to result in shippers B and C receiving worse service than otherwise would be the case, and may delay overall solution of the problem. Moreover, it is unlikely the Board (or any shipper) has any greater railroad operating knowledge than the railroads involved, thus, neither the Board nor shippers are well positioned to give advice to the railroads once service begins to collapse.

Nor is a set of penalties or incentives prescribed by the Board likely to improve the situation. No conceivable set of penalties or incentives that might be within the Board's power would provide the railroads any greater motivation to avoid disruption than has been provided by the markets following the service disruptions that have occurred in recent years.[10] Nevertheless, the implementation of these mergers was flawed and neither the railroads, the shippers, nor, indeed, the Board appears to have anticipated the deficiencies in the implementation arrangements, notwithstanding the Board's requirements that the railroads submit traffic projections and operating plans as part of their application. The Ports believe there are two implementation problems that need to be addressed in the supplementary guidelines.

First, the Board must recognize that in certain recent mergers it has effectively disabled itself from being in a position to review certain financial aspects of the transactions, and from adopting conditions that would significantly impair the value of the transaction to the applicant carriers. Where a transaction is for cash, the Board's practice of permitting the transaction to be closed into a voting trust pending final Board approval effectively precludes any meaningful review of the financial aspects of the deal, and the imposition of any conditions that might significantly affect the value of the transaction to the applicant carriers carries with it substantial risk of causing irreparable financial harm to the carriers involved. To put the matter in the context of the recent CSX/NS acquisition of Conrail, once $10 billion of cash was borrowed by CSX and NS and paid out to holders of Conrail stock, the Board simply lost the ability meaningfully to review the level of fixed charges that resulted from the transaction -- a review which is a statutory requirement. 49 U.S.C. 10324(b)(3). Moreover, after the money had been borrowed and spent, the Board could impose conditions that significantly affected the value of the transaction only at considerable risk to the financial viability of the applicants. This situation should not be permitted to occur in future transactions.

---

[10] It has been reported that the *combined market capitalization* of CSX and Norfolk Southern is now less than the price they paid for Conrail. The market penalty inflicted has simply wiped out the pre-transaction value of both the CSX and NS systems.

Second, the Board must recognize that in recent mergers there has been no detailed and effective critique of the applicants' traffic projections, traffic flows, operating plans and available assets from the perspective of plan implementation. The Board itself does not have the resources to perform that type of analysis, and none of the individual litigants in a merger proceeding has an adequate incentive to do the job itself and bring the results to the Board. As a practical matter, opposing railroads have little interest in ensuring a smooth implementation of the merger they are opposing. Shippers, who do have such an interest, have little interest in bearing the very substantial cost of such work of general applicability once their more particular problems are resolved by a negotiated contract or condition. The result has been that there is rarely an effective, in depth, challenge and analysis of the applicants' operating plans. This situation must be corrected.

The supplementary guidelines need to address both issues.

Cash Transactions:

Transactions involving two or more Class I carriers and involving the direct or indirect payment of cash to shareholders or the assumption of debt by one or both of the carriers must not be consummated prior to approval by the Board where the combined cash payment and debt assumption would exceed $500 million. The use of a voting trust in such circumstances frustrates the Board's statutory obligation to review the terms of the transaction and the level of debt that will result from the transaction, and effectively limits the scope of the Board's review of other aspects of the transaction.

Operating Plan Review:

Simultaneously with the submission of its Operating Plan pursuant to 49 CFR 1180.8, the applicants should be required to submit to the Board and serve on the parties to the proceeding, an analysis of that plan and a certification prepared by independent consultants acceptable to the Board. The independent consultants should certify that (a) the applicants have provided the consultants with full access to all data the consultants believe is necessary to conduct their review, (b) the consultants have reviewed and analyzed the traffic that is likely to be carried by the merged system and the traffic lanes in which it is likely to move, (c) the consultants have reviewed and analyzed the applicants' proposed operating plan and the assets and resources that the applicants will have to implement that plan, and (d) in the consultants' professional opinion the assets and resources of the combined carriers and the proposed operating plan will be adequate to serve the expected traffic, subject to such exceptions and qualifications as the consultants specifically list. Both the Board and the shippers should be entitled to rely on the consultants' analysis of the carrier's submissions. The objective is to bring the consultants as close to the position of financial auditors, and to subject them to the same incentives for thoroughness, accuracy and objectivity, as is possible under existing law.

Proposed Guidelines:

No transaction subject to these supplementary guidelines will be approved by the Board where the transaction has been structured, directly or indirectly, to result in a payment of cash or assumption of debt by one or more of the involved Class I carriers, or by one or more of their affiliates, prior to approval of the transaction by the Board, where the combined cash payment and debt assumption exceeds $500 million, unless specifically authorized by the Board.

Simultaneous with the submission of their operating plan pursuant to 49 CFR Part 1180, the Applicants in a transaction subject to these supplementary guidelines shall submit an analysis and certification of that plan prepared by an independent consulting firm, acceptable to the Board, which represents and certifies to the Board and to the shippers served by the Class I carriers involved:

(i) the Applicants have made available to the consultants all information the consultants consider necessary for their analysis;

(ii) the consultants have reviewed the Applicants' traffic projections, including projections of traffic volumes and traffic flows, and Applicants' operating plan and the assets available to the Applicants to implement the operating plan; and

(iii) in the consultants' professional opinion the Applicants' projections of traffic volumes and traffic flows are reasonable, and the operating plan and the assets available to the Applicants are adequate to serve the projected traffic volumes and traffic flows, subject to such exceptions and qualifications as the consultants specifically list.

CONCLUSION

The final round of mergers among North American railroads will present the Board with its last clear chance to ensure that the resulting rail system is one that serves the public interest. The key to a rail system that serves the public interest *over the long term* is to ensure that the final structure is one that provides meaningful rail-to-rail competition to all shippers where this is feasible. The supplementary guidelines the Ports have proposed will ensure that each covered transaction involving two or more Class I carriers will lead to a more competitive rail system that will better serve the long run interests of shippers and the public. The proposed supplementary guidelines should be incorporated into the Board's Notice of Proposed Rule Making.

Respectfully submitted:

THE PORT OF SEATTLE, WASHINGTON

By: Stephen A. Sewell
Its Managing Director -- Marine Division

THE PORT OF TACOMA, WASHINGTON

By: Andrea Riniker
Its Executive Director

THE PORT OF EVERETT, WASHINGTON

By: John M. Mohr
Its Executive Director

For the Port of Seattle:

Stephen A. Sewell

By: Stephen A. Sewell
Managing Director, Marine Division

PORT OF TACOMA

BY: Andrea Riniker

Andrea Riniker,
Executive Director

Ok Paul Chilcote

For comments of the Port of Seattle, Port of Tacoma and the Port of Everett regarding the Board's future Merger guidelines.

5/15/2000

Post-it™ brand fax transmittal memo 7671 | # of pages ▸ 1

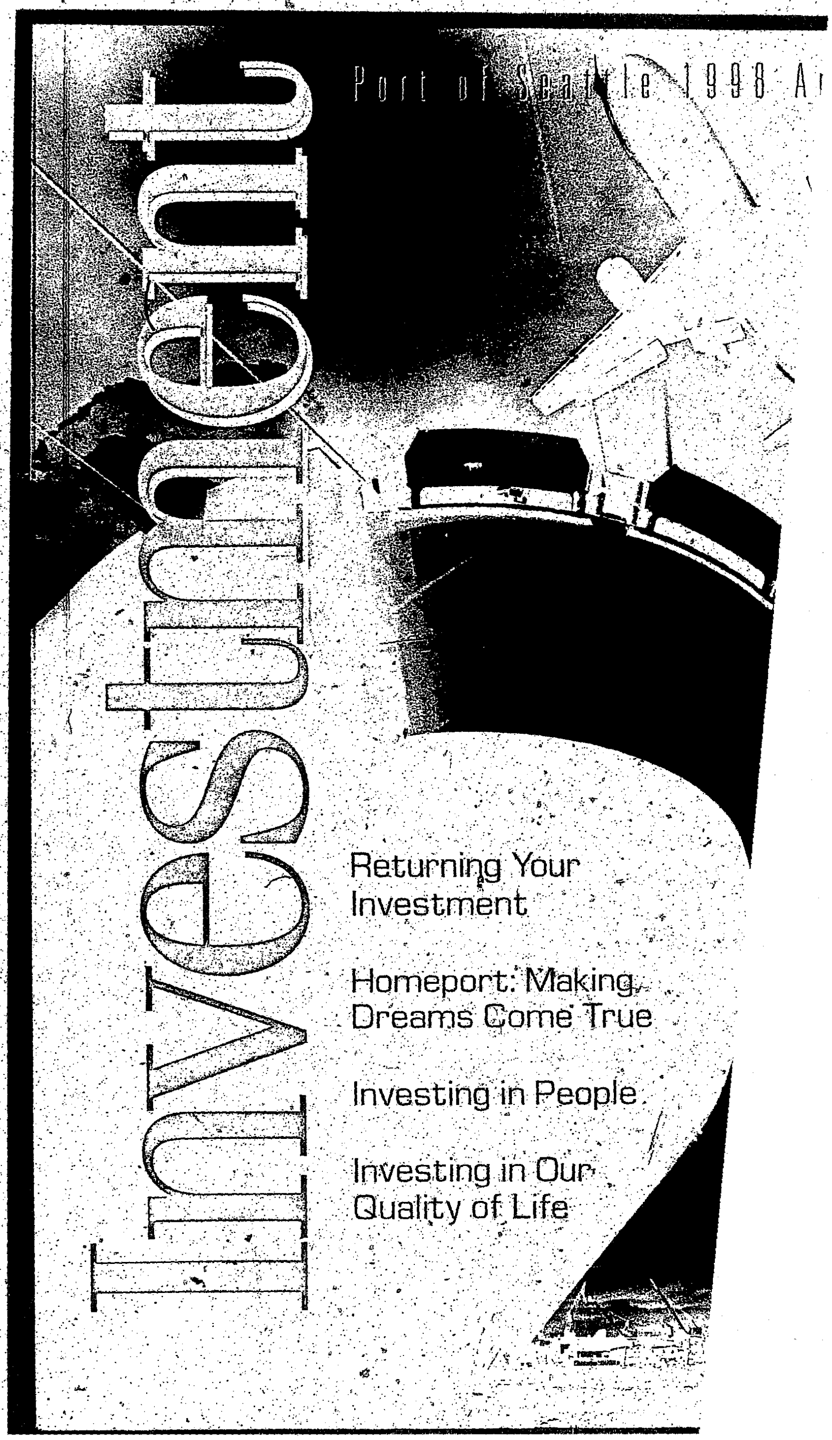
To John Bradley	From Paul Chilcote
Co.	Co. Port of Tacoma
202 333 6025	253-[illegible]
202 333 5686	253-[illegible]-7521

TOTAL P.01

By: [signature]
Port of Everett, Washington
It's Executive Director
John M. Mohr

ATTACHMENT No. 1

(Port of Seattle Annual Report)


Investment
Port of Seattle 1998 A
Returning Your Investment
Homeport: Making Dreams Come True
Investing in People
Investing in Our Quality of Life

Investment

As a community partner since 1911, the Port of Seattle takes a long-term interest in this region's economic health. To the Port, investment is about keeping King County on the cutting edge of global competition. That's why the Port makes major investments in its seaport and airport every year, keeping the long-term perspective on the world economy. Our investments are about creating family-wage jobs and about making our community a better place to live. This annual report is devoted to highlighting some of these investments — many of which came on-line this year.

Table of Contents

Vision and Mission

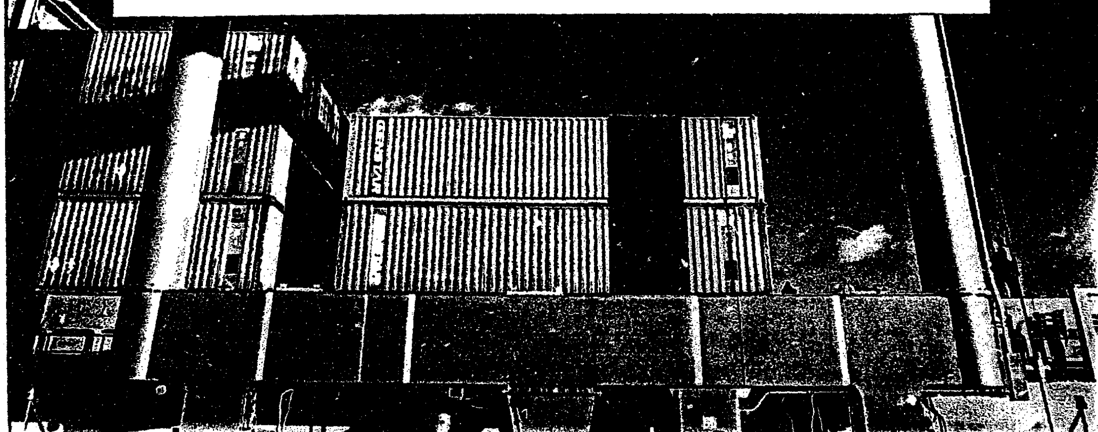
The Port of Seattle's vision is to be the most effective and respected provider of transportation facilities and services to promote international trade and commerce, and will be the best publicly owned catalyst for sustained regional prosperity in the nation.

Our primary mission is to be a leader in providing services and facilities to accommodate the transportation of cargo and passengers by air, water and land; to provide a home for the fishing industry, and to foster regional economic vitality and a quality life for King County citizens.

The Port will also pursue other opportunities if they enhance its ability to achieve its primary mission or if they preserve scarce land resources — marine or aviation — of unique value for port uses.

In accomplishing its goals, the Port will work as a partner with other public and private entities. The intent is to complement, rather than duplicate or compete with, the functions of general purpose governments or the private sector.

Port of Seattle



President's Message

When Vice President Al Gore dedicated the new state-of-the-art container-shipping facility at Terminal 5 in Seattle in September, he praised the Port of Seattle for its commitment to creating new economic opportunities for our community in the global economy.

That event was just one of many in 1998 that reflect the Port of Seattle's mission and approach to investment in the community. We aim to deliver marine and aviation services and facilities that strengthen our region's competitive position in the United States and throughout the world.

In recognition of our prominent role in international trade, Seattle was chosen as the site for this fall's World Trade Organization Ministerial meetings. The eyes of the world will be on Seattle, as these meetings bring together leaders from more than 160 nations to make decisions on critical trade issues.

At Seattle-Tacoma International Airport, we continue to make progress toward our goal of meeting the needs of passengers and airline customers for expanded capacity and improved services. The airport set another record last year for air travel and air-cargo handling — yet again confirming the wisdom of our region's decision to expand the airport and making it even more essential that we move forward as quickly as possible.

The marine port also saw record cargo-container volumes in 1998. That was an outstanding achievement in a year when our Asian trading partners continued to feel the effects of a major economic downturn.

As we approach a new century, the Port's commitment to investment in the community becomes more critical to sustaining our region's economic vitality. As a government agency, the Port has responsibilities to represent the interests of King County citizens. The Port also is a service-driven enterprise dedicated to providing the modern facilities our customers need to move cargo and passengers efficiently.

As an example, the Port and Norwegian Cruise Line signed a four-year agreement that will make our nationally recognized Bell Street Pier the home port for weekly cruises to Alaska starting in May 2000. This achievement was possible only with the support of our partners in the private sector, labor and government over more than a decade to expand the cruise business in Seattle.

Our economic-development activities extend throughout King County. These efforts include partnerships in Bellevue and south King County to recruit new businesses and assist the expansion of existing companies. We also saw gains in 1998 to expand job-training and apprenticeship opportunities in collaboration with local government, business and labor.

Everyone in our community shares a responsibility for the education of our young people. The Port is proud of its accomplishments in 1998 to expand awareness of the importance of trade and help our students prepare for exciting careers in trade and transportation.

The Port's effort to upgrade our area's transportation infrastructure is another example of how we work collaboratively to attain regional goals. Improving roadway and railway links will speed the movement of people and goods — and also ease traffic congestion, reduce air pollution and make our roadways safer.

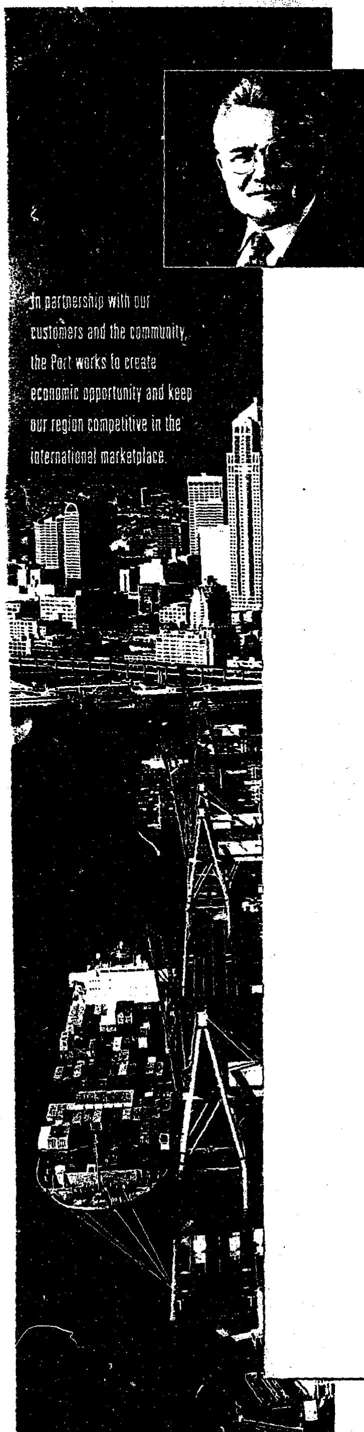
As a leading international gateway, the Port provides access to world markets for many leading Washington state businesses. Our rising trade flows help sustain a thriving transportation industry comprised of hundreds of companies employing thousands of workers throughout the region. In this way, the Port serves to diversify our economy and cushion the impact of any economic downturns.

The Port's unique role and mission give us the opportunity to engage in activities that other local governments cannot do, and that private enterprise may be unable to do. These activities may not produce results immediately to the Port's bottom line — but the investments pay for themselves many times over in new jobs, economic opportunities and an improved quality of life in our community.

As we look ahead to the new century, we can do so with confidence because of the dedication of our Port staff and labor force. Their commitment to the community makes our accomplishments possible.

Patricia Davis
Patricia Davis, President
Port of Seattle Commission

Gary Grant, Commissioner · Patricia Davis, President · Jack Block, Vice President · Paige Miller, Secretary · Clare Nordquist, Assistant Secretary



Executive Director's Message

The core values of our region — innovation, a commitment to community and respect for the environment — provide the foundation upon which our strong economy and quality of life are built. These, too, are the values that guide the Port of Seattle as we make investments in world-class marine and aviation facilities to meet our region's trade and transportation needs well into the next century.

In partnership with our customers and the community, the Port works to create economic opportunity and keep our region competitive in the international marketplace. With one of every four jobs in Washington tied to international trade, the Port's role in providing access to world markets becomes even more critical. A new example of the Port's service to the region as a catalyst for economic development was the opening last October of the World Trade Center on the Central Waterfront.

The Port completed the Terminal 5 expansion for APL Ltd. and its alliance partners in 1998, and launched the Terminal 18 expansion on Harbor Island this year. These major projects make Seattle well-positioned to accommodate the large new ships operating in the trans-Pacific trade, as well as increased cargo volumes in the future.

Substantial progress occurred last year in the planning at Seattle-Tacoma International Airport for improvements to the terminal, parking facilities, drives and airfield. As these major projects move forward, the Port is committed to maintaining the excellent service our airline customers and passengers expect.

The Port's responsibility to create economic opportunity extends well beyond our harbor and airport. To prepare our young people for the challenging jobs of the future, business, labor and our educational institutions work as a team to develop creative approaches to workforce training. In my role as Chair of the Governor's Task Force on School-to-Work Transition, I have been rewarded by the enthusiastic response from many students and teachers as we open the doors to exciting careers in trade and transportation.

The Port, as a steward of our natural resources, is committed to protection of the environment as we expand our aviation and marine facilities. In particular, the Port is closely involved with local, state, tribal and federal governments and other stakeholders in Endangered Species Act compliance.

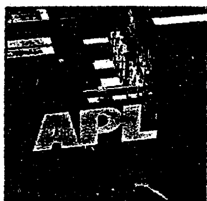
As operators of vital infrastructure, the Port also has dedicated substantial resources to addressing Year 2000 concerns. We have identified critical systems in our aviation and marine operations and have developed comprehensive remedial and testing plans, including contingencies for possible external Y2K failures.

Thomas M. Tierney, Jr., Chief Administrative Officer/Chief Financial Officer
Gina Marie Lindsey, Managing Director, Aviation Division
Stephen Sewell, Managing Director, Marine Division
Linda Strout, General Counsel
Mic Dinsmore, Executive Director

Ensuring a continued high level of service to our customers also has guided the Port's efforts to improve the region's transportation system. The Port has joined in partnership with the private sector, local communities, the state and federal agencies to separate road and rail traffic at several key bottlenecks, including SR 519 in Seattle's industrial area and in south King County communities.

It takes people to put these goals and priorities into action. I am particularly gratified by the increased involvement of our employees in community giving efforts and volunteerism over the past year. Every day, and in many ways, the people of the Port of Seattle demonstrate their commitment to the community.

M.R. Dinsmore
Executive Director
Port of Seattle



Returning
Your Investment

Veteran marine clerk Jackie Annibal remembers how she used a pencil and paper to track containers at Terminal 5. But that was before the Port of Seattle and its partner APL spent hundreds of millions of dollars to expand the operation and turn it into one of the world's most efficient container terminals.

Today, the boxes show up in color-coded charts on her computer screen. She can tell instantly where the cargo is and where it needs to go. Together with new on-dock rail service, Annibal's access to computer technology has boosted the terminal's efficiency three-fold. It used to take an hour to get a container from ship to train. Now it takes 20 minutes.

Every day, the Port's strategic expansion of Terminal 5 and its other marine facilities keeps this community on the cutting edge of the fiercely competitive shipping industry. The same is true of the Port's position in the aviation industry, with its expansion of Seattle-Tacoma International Airport.

Every year, the Port, its labor partners and business customers make long-lasting investments in transportation, productivity and technology at the seaport and airport. The Port alone plans to spend $2.3 billion during the next five years to create assets that help King County citizens strengthen their communities as a major crossroads for international trade and travel. Here is how your investment did in 1998.

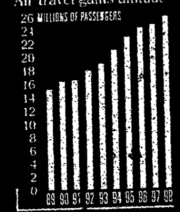
Sharpening Our Competitive Edge

The Port of Seattle is one of the world's most important centers for global waterborne commerce. However, the shipping industry is changing rapidly, and the Port needs to stay ahead of the game. With the completion of Terminal 5, the planned expansion of Terminal 18 and proposed upgrades to Terminals 25, 30, 37 and 46, the Port keeps up with a growing demand for larger, more efficient container terminals. Shipping lines have responded to the Port's investments with a vote of confidence. Even before Terminal 5 was officially dedicated on Sept. 13, APL and its New World Alliance partners made Seattle first port of call for one of its services to Asia.

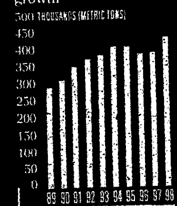
"Global Gateway North (T-5) is part of our two-hub strategy on the West Coast," APL President Tim Rhein said. "Together with our Global Gateway South in Los Angeles, this terminal positions us to provide speed and reliability."

(Continued on page 8)

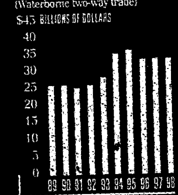
Air travel gains altitude



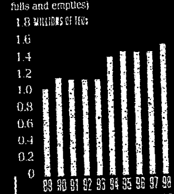
Air cargo resumes growth



Trade remains stable
(Waterborne two-way trade)



Containers increase
(All figures in 20-foot equivalent units, fulls and empties)

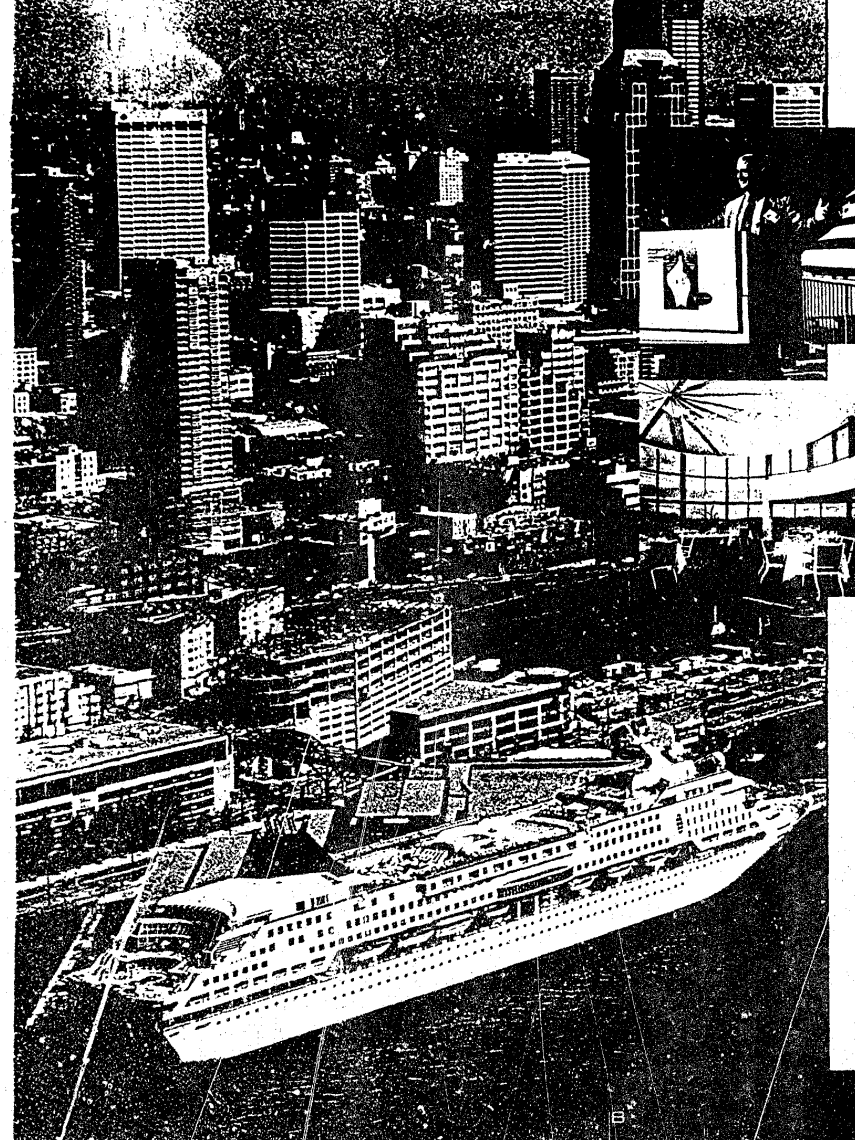


Homeport: Making Dreams Come True

It's the Klondike all over again, said Seattle Mayor Paul Schell as he summed up one of the year's most significant announcements for the regional economy.

For decades, many at the Port and in Seattle's business community had worked [illegible] to attract the fast-growing cruise industry and see the new "ships of [illegible] here in Seattle.

[illegible] 1998, on the rooftop of Bell Street Pier with one of their giant [illegible] them, executives from Norwegian Cruise Line made our dream [illegible] announced NCL will begin using the Port of Seattle's Pier 66 as a [illegible] summer cruises to Alaska in May 2000. The four-year agreement is [illegible] more than 400 new jobs, pump $74 million into the economy and [illegible] 3.4 million in government taxes.



Returning
Your Investment

(Continued from page 6)

APL's Asian service wasn't the only new business the Port captured in 1998. Several major national retailers, concerned about congestion in Southern California and impressed by Seattle's efficiency, decided to switch their Asian imports to Seattle. The Port also began making an investment to capture new business at Terminal 91, its primary break-bulk complex. The terminal's multi-million-dollar renovation will position Seattle to win more project cargo — items that are too large or too heavy to fit in containers, such as farm machinery, road-building equipment, boats and motor homes.

Creating a World-Class Airport

In 1998, about 25.8 million passengers passed through Seattle-Tacoma International Airport. That's almost the equivalent of the entire population of Canada. Sea-Tac Airport was designed in the 1970s to handle only 25 million. In short, the busiest airport in the Pacific Northwest is bursting at the seams. Last year, the Port took some big steps in a five-year, $1.5 billion journey that will give Sea-Tac a World Class Upgrade. The airport will have 3,000 new parking spaces, an all-weather third runway, new terminal facilities, an expanded concourse, new vendors, a new control tower and much more.

To fund the airport's expansion, the Port became one of the first airports in the nation to issue long-term bonds backed solely by passenger fees. This means the Port obtained $260 million in financing without using its own credit or that of its airline customers, thus preserving its revenue bond capacity for other airport projects.

To begin creating more room for passengers and airlines, the Port last year broke ground for the new parking garage and kicked its third runway property acquisition program into high gear. It moved 55,000 truckloads of dirt for construction, and began work on taxiways for the new runway. The investment didn't stop there. To help make air travel safe at the turn of the millennium, the Port also spent millions of dollars to make its computer systems Y2K compatible.

"We're excited to be part of an airport that's undergoing such major improvements," said Bob Johnston, general manager for American Airlines at Sea-Tac. "The World Class Upgrade bodes well for our customers."

Paving the Way for Global Commerce

In November 1999, ministers from 133 nations will come to Seattle for the next round of global trade talks under the World Trade Organization. Seattle's successful bid to host the event is another indication that our state has become an international crossroads.

To help local companies tap into that potential for new trade opportunities and help boost King County's position as a center for global commerce, the Port opened the 70,000-square-foot World Trade Center (WTC) Seattle in October 1998. The Port's corporate partners — Boeing, Weyerhaeuser, Microsoft, Seafirst, US West and United Airlines — co-founded WTC Seattle, which has more than 600 members. The center, part of a network of 306 centers in 92 countries and home for 10 local non-profit international organizations, is across the street from the Bell Harbor International Conference Center where some of the WTO meetings will take place.

"World Trade Center Seattle will help us to focus our strength and energies to capture countless opportunities all of us have in the global economy," Boeing CEO Phil Condit said. "It's time for Seattle to show new leadership in world trade."

Investing in People

Every week, Larry Hansen, Randy Brown, Joe Toro, Ken Passe, Sean Pierce, Kelly Garber and John Swanson file into a meeting room at Port headquarters on Pier 69 and sit down for several hours to talk about their work on the waterfront.

This may not sound like a big deal until you consider who these men are. Larry, Joe and Randy are officials of the International Longshore and Warehouse Union. Ken, Sean and Kelly represent the companies that run the Port's container terminals — Marine Terminals, TraPac and APL respectively. John is the Port's director of labor relations. Together, they form the communications committee of the Seattle World Class Port Coalition, a unique labor-management team-building effort.

Until about a year ago, having all of them in one room would have seemed extraordinary. Following tense labor negotiations in late 1997, relations between labor and management — not to mention morale and productivity — hit bottom, and traditional mediation efforts were going nowhere.

Then, the Port stepped in and tried something new. It brought together everyone from the working waterfront in a safe environment so they could begin to know and trust each other. The goal was to work together to boost efficiency and make sure Seattle remains one of the most productive ports on the West Coast.

It worked. After a year of meetings that cover everything from traffic snarls to new technology, productivity at the Port has shot up to 28 container moves per hour, one of the highest standards on the coast.

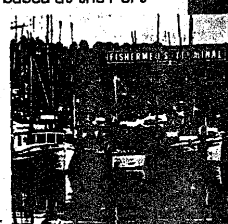
The creation of the Seattle World Class Port Coalition shows the Port is as passionate about investing in people as it is about expanding the facilities that make this region's economy hum.

Providing Jobs

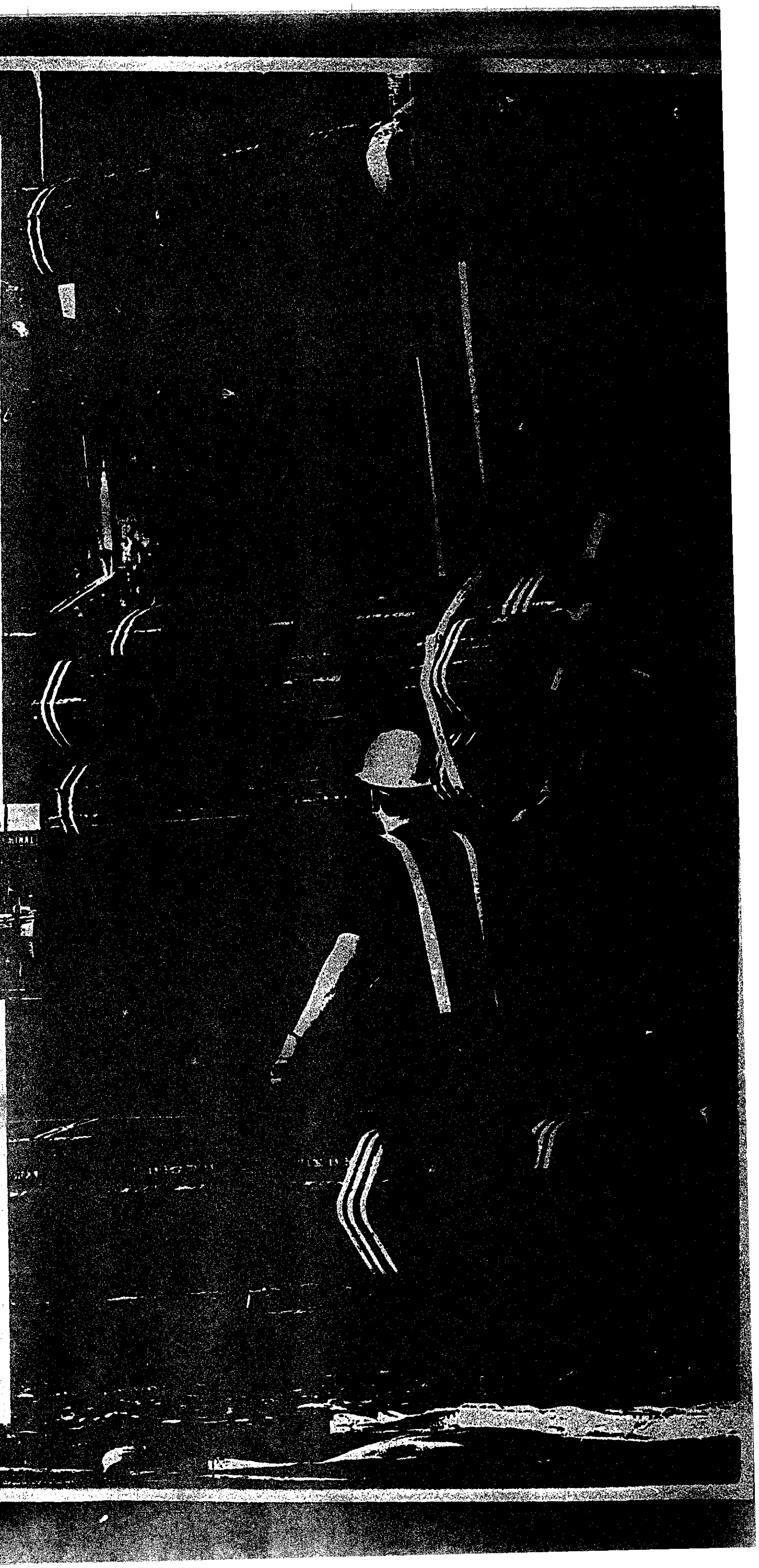
Through the Office of PortJOBS, which is funded by the Port, the City of Seattle, King County and the private sector, the Port supported the Seattle Conservation Corps to provide the equivalent of 40 full-time jobs for homeless adults. Under the three-year, $1 million agreement, Corps members will work on a number of projects, including helping construct and landscape public access sites at the Port's Terminal 107.

Sustaining Communities

It is no secret to anyone in the Puget Sound area that the fishing industry is a vital but struggling part of our economic community. In particular, the number of operators of smaller boats has decreased in recent years. Yet the North Pacific fishing fleet — based at the Port of Seattle's Fishermen's Terminal — continues to provide a livelihood to many families, while its traditions are woven into the region's social and cultural fabric.



To help support 700 fishing families and their industry, the Port last year set out to keep their home base economically viable by marketing vacant moorage space to commercial work boats. The program has been a success, attracting more than 30 non-fishing tenants ranging from salvage boats and tugs to tour boats and charter boats.



Investing
in Our Quality of Life

When the sun rises above Bell Street Pier, strollers climb to the rooftop to take in the commanding view of the Seattle waterfront. Diners wander outside to tables on the deck at Anthony's Pier 66 & Bell Street Diner to watch pleasure boats at Bell Harbor Marina. Conferees at Bell Harbor International Conference Center glance at the glistening expanse of Elliott Bay. Children emerge from Odyssey — Maritime Discovery Center and dart across the public plaza.

There's no question: Bell Street Pier is alive.

But it didn't used to be that way. Until 1985, when the Port Commission took the bold move to renovate and spur $310 million in private development around it, Pier 66 was steeped in neglect, disrepair and polluted sediment.

To recognize the vision that turned dereliction into opportunity and produced a crossroads of commerce, recreation and education, the American Association of Port Authorities awarded the Port its 1998 Environmental Enhancement Award.

Bell Street Pier is part of a bigger trend. In recent years, the Port has complemented its role of providing regional transportation facilities with other efforts to make King County a better place to live. That translates into investments in everything from a vibrant downtown waterfront to recycling landscape debris at 20 public access sites the Port owns.

Tender love and care for Mother Nature shows up everywhere the organization interacts with the environment we live in. At the airport, workers managed to cut the amount of hazardous waste from maintenance cleansers and other materials last year to 8,000 pounds from 12,400. Terminal 5, formerly a national Superfund cleanup site, has become a productive community asset with a 13-acre public access site *The Seattle Times* described as a "waterfront wonder." Shilshole Bay Marina works with its live-aboard moorage customers to promote proper sewage handling and keep Puget Sound clean for all users.

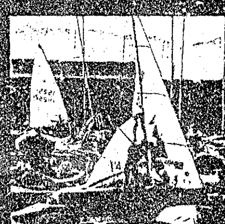
Last year, the Port expanded its responsibility as a corporate citizen to help keep this community one of the best places in the country to live and work.

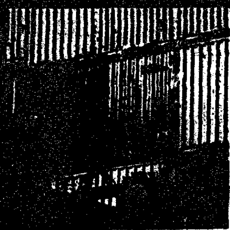
Bringing the World to the Classroom

For 150 Seattle-area middle school students, international trade is something they can get their hands on. They helped Mitsubishi manager Mark Shiroishi market Washington state vegetables to Japan in the midst of the Asian economic crisis, for instance.

They know about Shiroishi because of the Journeys Project, a unique educational initiative to help students learn about global commerce and their community's role in it.

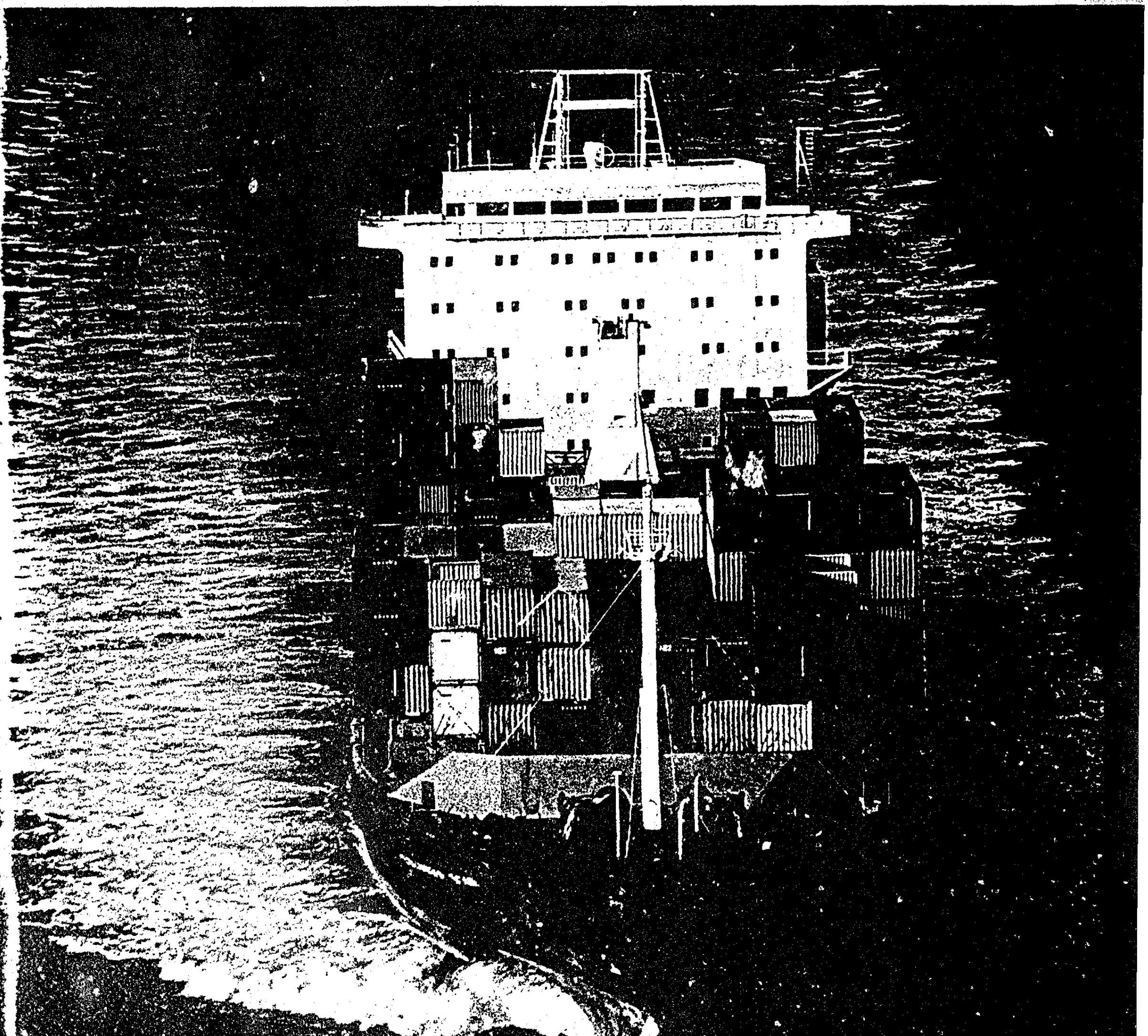
The project, sponsored by Mitsubishi International Corporation, the Port, Metropolitan King County and a number of other community partners, is one example of how the Port helps cultivate a new generation of King County residents savvy about the global economy on which they depend.





Marine
Operational Highlights

- The Port of Seattle handled 1.54 million TEUs in 1998 — a 4.6-percent increase over those in 1997 and a new record in container volume.
- The rise in cargo traffic was the result of a surge in imports and the diversion of cargo from California ports by importers concerned about congestion. Specifically, the increase in traffic came from higher-than-expected growth at the United Alliance at Terminal 46 and a new vessel rotation by the New World Alliance at Terminal 5.
- Early in the year, the Port initiated the formation of the Seattle World Class Port Coalition. The unique labor relations efforts between the International Longshore and Warehouse Union, the Pacific Maritime Association and the Port helped boost container productivity to 28 moves per hour, a 47-percent increase over those in 1997.
- The Marine Division completed the Terminal 5 expansion project early. APL's cutting-edge "Global Gateway North" was dedicated on Sept. 13, bringing on line the second-largest container terminal on the West Coast.
- The Division also completed the design for an expanded Terminal 18. The two-year project is scheduled to begin in 1999. It will double the facility's size and expand its on-dock rail capacity.
- As a result of the Asian financial crisis, grain exports from Terminal 86 declined significantly. The Division identified imported fruit business from South America as a new area of market focus.
- Contractors completed the first phase of the apron replacement program at Terminal 91 to make up for 20 years of deferred maintenance and prepare the facility for another target market: heavy equipment and project cargo trade.
- Norwegian Cruise Line announced it will begin using Bell Street Pier as a homeport for summer cruises to Alaska in May 2000. The Division launched the design process to build out the cruise terminal space at Pier 66. Bell Harbor Marina increased overnight stays at the recreational boating facility by 30 percent.
- The Port opened the World Trade Center project on Seattle's central waterfront. The fourth floor is home to the worldwide World Trade Center Seattle franchise and 10 international non-profits.
- To keep Fishermen's Terminal viable for the North Pacific fishing fleet, facility managers stepped up our program to attract commercial work boats. Owners of 30 non-fishing vessels signed up as new tenants as a result.
- Shilshole Bay Marina secured two new tenants — the Marina Club and Admiralty Yacht Brokers — for the main building, and opened a new 60-foot dock.
- Warehousing and distribution signed up a large customer, and relocated the Foreign Trade Zone to Terminal 104 from Harbor Island. The FTZ facility saw its business grow significantly after the move.



February 1, 1998
Port, labor and industry form Seattle World Class Port Coalition.

September 13, 1998
Vice President Al Gore attends dedication of Terminal 5 with APL.

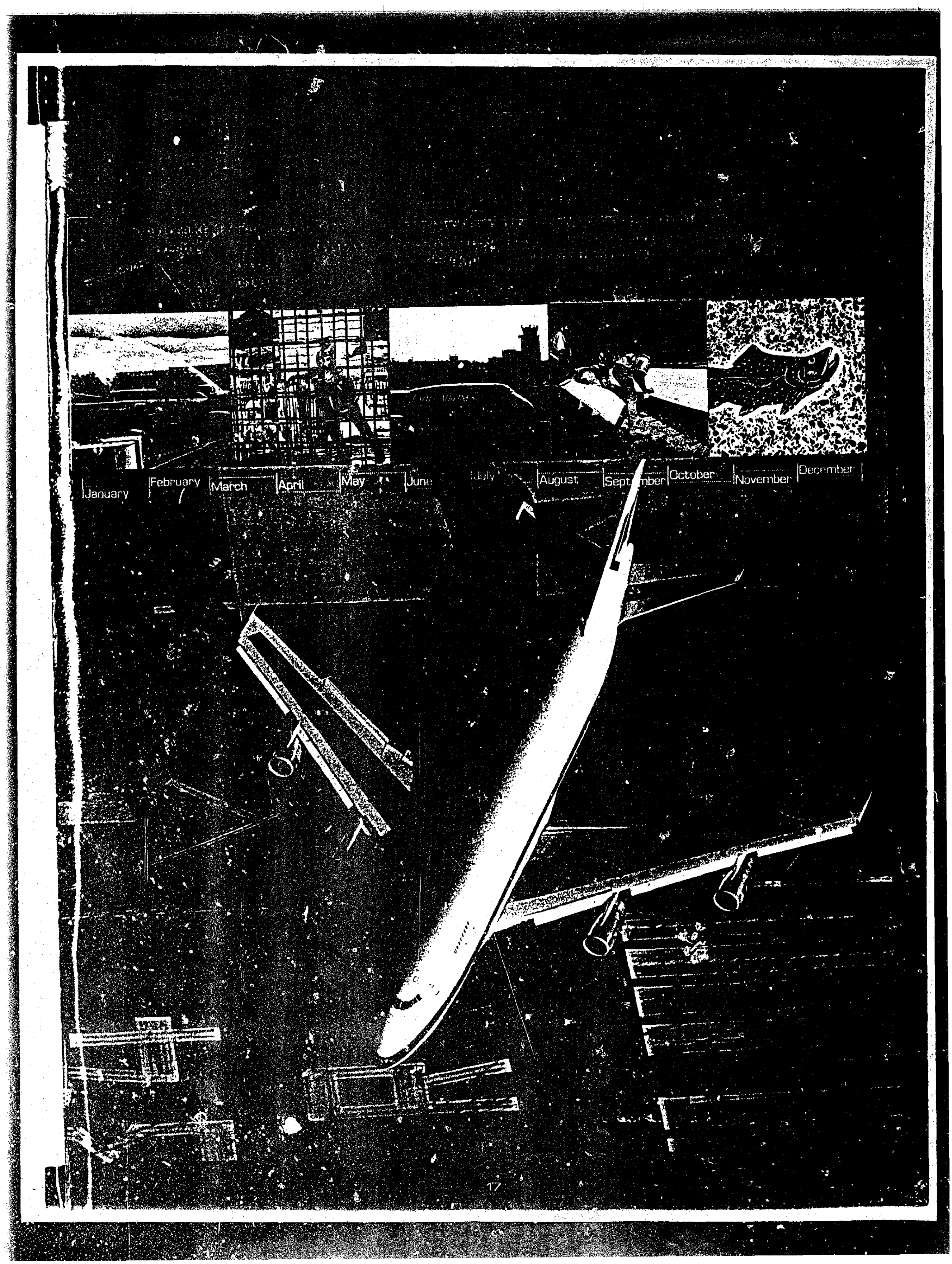
September 15, 1998
Norwegian Cruise Line announces agreement to use Seattle as cruise ship homeport.

October 6, 1998
Port opens World Trade Center West building.

January | February | March | April | May | June | July | August | September | October | November | December

Aviation
Operational Highlights

- For the 16th year in a row, Seattle-Tacoma International Airport set a record for passenger traffic, handling 25.8 million passengers and exceeding its design capacity of 25 million passengers for the first time. Overall, 1998 saw an increase of more than a million passengers over those in the previous year, with a 16.8-percent increase in international traffic.
- Air cargo grew by almost nine percent to 428,272 metric tons.
- The Federal Aviation Administration approved a precedent-setting application by the Port of Seattle to collect more than $1 billion in airline passenger fees during the next five years. These funds will be used to pay for capital projects and service the debt on an innovative $262-million bond issue backed solely by the passenger facility charges. The bond issue will provide partial funding for many key airport projects, including the third runway and south terminal expansion.
- Sea-Tac's Capital Improvement Plan began in earnest with more than $200 million in construction spending completed in 1998. Projects included:
  - The newly rebuilt south airport entrance roadway, improving the connection to the airport drives.
  - Beginning of a $53-million expansion of the airport garage, which, when completed in 2000, will increase parking capacity by almost a third.
  - Completion of strengthening of ramps and drives around the Sea-Tac parking garage and terminal to better withstand earthquakes. Construction also began on a new ramp from the check-in drive to the fourth level of the parking garage.
  - Completion of main terminal lighting improvement project.
  - The movement of more than 900,000 cubic yards of earth for the third runway, representing about nine percent of the material that needs to be brought to the construction site.
- Sea-Tac celebrated the inaugural flight of United Airlines' daily non-stop Seattle-Tokyo service, flights made possible by a new aviation agreement between the United States and Japan.
- Northwest Airlines and KLM Royal Dutch Airlines launched new daily non-stop service between Seattle and Amsterdam.
- Sea-Tac continues to be a national leader in managing aircraft noise, installing noise insulation in more than 1,000 homes in 1998.
- For the second straight year, Sea-Tac received a perfect score from the Federal Aviation Administration on its comprehensive safety and security inspection. Sea-Tac is the only airport in the nation to have passed this operating inspection two years in a row with zero defects.


January
February
March
April
May
June
July
August
Sept mber
October
November
December

General
Highlights

Looking Back, Looking Ahead

The Port of Seattle is a public enterprise that operates in a market-driven international environment. Owned by the citizens of King County, the Port provides services to its customers in the maritime and aviation industries.

These services return benefits to the people and businesses of the county and the region. They include expedient, reliable and low-cost connections by land and sea with the rest of the world. And, they include the social and economic benefits of job creation, environmental cleanup and long-term regional economic security stemming from careful management of the community's investment in the Port.

In 1998, the Port continued to cover the cost of its operations using revenues from aviation and marine industry customers. The Port's two operating divisions each earned positive net revenues after depreciation and administrative allocations. Combined net operating cash flow increased to $89.9 million despite the challenges of the Asian economic crisis.

Besides funding major capital projects through its operating income, the Port also invested in non-aviation capital assets through a tax levy on property in King County. The levy is used for public access and road construction, environmental improvements and job-producing marine terminal development. The levy is not used for aviation investments or to cover operating expenses.

In 1998, the Port Commission decided to lower the levy rate for 1999 for the seventh year in a row, adding up to a saving in the tax rate of 30 percent since 1992. In 1998 alone, Commissioners trimmed the tax rate by nine percent.

The levy for a $200,000 house in 1999 is $48, compared to $53 in 1998.

Cutting the tax rate during most of the decade means the Port has foregone levying about $126 million in taxes.

Looking forward, the Port's net operating income is expected to grow by an additional 13 percent in 1999. The 1999 capital budget is projected to reach $368 million, an eight-percent increase over that in 1998. This is part of a five-year, $2.3-billion capital improvement plan for Sea-Tac Airport and seaport projects. The 1999 budget reflects two main priorities: upgrading the airport to better serve passengers and accommodate growth in air travel, and improving the region's transportation network to speed the movement of cargo and ease congestion.

Independent Auditors' Report

Port Commission
Port of Seattle
Seattle, Washington

We have audited the accompanying balance sheets of the Port of Seattle (the Port) as of December 31, 1998 and 1997, and the related statements of operations, equity, and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the Port's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Port of Seattle as of December 31, 1998 and 1997, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

As discussed in Note 1 to the financial statements, in 1998 the Port changed its method of accounting for investments to conform with Governmental Accounting Standards Board Statement No. 31 and retroactively restated the 1997 and 1996 financial statements for the change.

As discussed in Note 1 to the financial statements, the Port changed its method of accounting for its deferred compensation plan in 1998.

The year 2000 supplementary information on page 40 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board, and we did not audit and do not express an opinion on such information. Further, we were unable to apply to the information certain procedures prescribed by professional standards because of the unprecedented nature of the year 2000 issue and its effects, and the fact that authoritative measurement criteria regarding the status of remediation efforts have not been established. In addition, we do not provide assurance that the Port of Seattle is or will become year 2000 compliant, that the Port of Seattle's year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Port of Seattle does business are or will become year 2000 compliant.

Deloitte & Touche LLP

Deloitte & Touche LLP
Seattle, Washington
March 10, 1999

Balance Sheets
(In thousands)

December 31,	1998	1997
ASSETS		
LAND, FACILITIES, AND EQUIPMENT, at cost	$ 2,405,289	$ 2,158,047
Less accumulated depreciation	578,936	518,576
	1,826,353	1,639,471
Construction work in progress	214,211	146,339
Cash and cash equivalents restricted for debt service and acquisition of land, facilities, and equipment	193,239	226,106
Investments and accrued interest restricted for debt service and acquisition of land, facilities, and equipment	239,450	105,079
	2,473,253	2,116,995
DEFERRED FINANCE COSTS, net of accumulated amortization of $4,981 and $3,835	15,764	4,443
CURRENT ASSETS:		
Cash and cash equivalents, including restricted amounts of $7,120 and $5,507	97,034	56,796
Investments	250	52,186
Accounts and contracts receivable, less allowance of $944 and $653 for doubtful accounts	25,689	21,633
Federal grants-in-aid receivable	17,276	4,717
Taxes receivable	1,085	1,100
Maintenance supplies	4,269	4,021
Prepayments and other current assets	642	661
Total current assets	146,245	141,114
TOTAL	$ 2,635,262	$ 2,262,552

See notes to the financial statements

EQUITY AND LIABILITIES

December 31,	1998	1997
EQUITY FROM:		
Operations	$ 190,380	$ 184,049
Taxation	843,930	781,968
Grants and donations	273,566	241,963
	1,307,876	1,207,980
COMMITMENTS AND CONTINGENCIES (Notes 8 and 9)		
LONG-TERM DEBT, less current maturities:		
Revenue bonds	720,350	754,750
General obligation bonds	141,300	148,685
Passenger facility charges revenue bonds	262,500	
Notes payable	451	650
Capital appreciation bonds	4,387	3,741
Unamortized bond discount, net of accumulated amortization of $12,866 and $11,265	(13,791)	(18,916)
	1,115,197	888,910
LONG-TERM LIABILITIES:		
Accrued environmental expenses	12,300	11,425
CURRENT LIABILITIES:		
Warrants outstanding	13,381	5,158
Accounts payable and accrued expenses	22,514	39,214
Payroll and taxes	19,342	50,365
Bond interest payable	13,248	10,555
Lease deposits and customer advances	3,449	2,940
Current maturities of long-term debt	127,955	46,005
Total current liabilities	199,889	154,237
TOTAL	$ 2,635,262	$ 2,262,552

Statements of Operations

(in thousands)

Years ended December 31,	1998	1997	1996
REVENUES:			
Services	$ 125,980	$ 121,394	$ 109,557
Property rentals	117,061	106,047	100,354
Total revenues	243,041	227,441	209,911
OPERATING EXPENSES:			
Operations and maintenance	132,681	124,872	109,746
Administration	19,892	18,871	18,237
Environmental	575	(4,204)	961
Total operating expenses before depreciation	153,148	139,539	128,944
Depreciation	64,098	54,369	51,103
Total operating expenses	217,246	193,908	180,047
Operating income	25,795	33,533	29,864
OTHER INCOME (EXPENSE):			
Revenue bond interest	(31,474)	(25,946)	(25,126)
Other income	8,818	4,884	11,919
Total other expense, net	(22,656)	(21,062)	(13,207)
Excess of revenue over expense before taxation, passenger facility charges and general obligation bond interest	3,139	12,471	16,657
TAXATION, PASSENGER FACILITY CHARGES AND GENERAL OBLIGATION BOND INTEREST:			
Ad valorem tax revenue	35,515	35,489	35,445
General obligation bond interest	(8,291)	(3,270)	(2,116)
Passenger facility charges	33,664	33,125	32,035
Passenger facility charges revenue bond interest	(89)		
Total taxation, passenger facility charges and general obligation bond interest	60,799	65,344	65,364
EXCESS OF REVENUE OVER EXPENSE	$ 63,938	$ 77,815	$ 82,021

See notes to the financial statements

Statements of Equity

(in thousands)

Years ended December 31, 1998, 1997, and 1996	Operations	Taxation	Grants and donations
BALANCE, January 1, 1996	$ 147,340	$ 652,138	$ 217,326
Ad valorem tax levy, including supplements and cancellations		35,445	
Excess of revenue over expense before taxation, passenger facility charges revenue, and general obligation bond interest	16,657		
General obligation bond interest		(2,116)	
Transfer of interest income associated with passenger facility charges revenue	(1,941)	1,941	
Passenger facility charges revenue		32,035	
Federal grants-in-aid funds			16,305
Transfer of depreciation on passenger facility charge assets	2,655	(2,655)	
Transfer of depreciation on federal grant assets	3,374		(3,374)
BALANCE, December 31, 1996	168,085	716,788	230,257
Ad valorem tax levy, including supplements and cancellations		35,489	
Excess of revenue over expense before taxation, passenger facility charges revenue, and general obligation bond interest	12,471		
General obligation bond interest		(3,270)	
Transfer of interest income associated with passenger facility charges revenue	(2,902)	2,902	
Passenger facility charges revenue		33,125	
Federal grants-in-aid funds			15,035
Transfer of depreciation on passenger facility charge assets	3,066	(3,066)	
Transfer of depreciation on federal grant assets	3,329		(3,329)
BALANCE, December 31, 1997	184,049	781,968	241,963
Ad valorem tax levy, including supplements and cancellations		35,516	
Excess of revenue over expense before taxation, passenger facility charges revenue, and general obligation bond interest	3,139		
General obligation bond interest		(8,291)	
Transfer of interest income associated with passenger facility charges revenue	(4,698)	4,698	
Passenger facility charges revenue		33,664	
Passenger facility charges revenue bond interest		(89)	
Federal grants-in-aid funds			35,957
Transfer of depreciation on passenger facility charge assets	3,536	(3,536)	
Transfer of depreciation on federal grant assets	4,354		(4,354)
BALANCE, December 31, 1998	$ 190,380	$ 843,930	$ 273,566

See notes to the financial statements

Statements of Cash Flows

(In thousands)

Years ended December 31,	1998	1997	1996
OPERATING ACTIVITIES:			
Operating income	$ 25,795	$ 33,533	$ 29,864
Adjustments to reconcile operating income to cash provided by operating activities:			
Depreciation	64,098	54,369	51,103
Nonoperating income (expense)	1,078	1,329	(479)
Cash provided (used) by changes in operating assets and liabilities:			
Accounts and contracts receivable	(4,056)	(2,943)	396
Maintenance supplies	(248)	(158)	17
Prepayments and other current assets	19	(43)	(72)
Accrued environmental expenses	875	(98)	(1,792)
Warrants outstanding	8,223	482	560
Accounts payable and accrued expenses	(16,700)	12,340	4,300
Reduced by accounts payable related to capital activities	18,329	(19,899)	1,134
Payroll and taxes	582	6,370	3,965
Lease deposits and customer advances	509	940	446
Net cash provided by operating activities	98,504	86,222	89,442
CAPITAL AND RELATED FINANCING ACTIVITIES:			
Proceeds from sale of passenger facility charges revenue bonds	260,304		
Proceeds from sale of revenue bonds	94,462	251,614	103,162
Proceeds from issuance of commercial paper	73,641		
Proceeds used for the refunding of revenue bonds	(94,880)		
Acquisition and construction of capital assets	(357,837)	(261,645)	(207,397)
Principal payments on revenue bonds	(32,920)	(29,410)	(29,180)
Principal payments on general obligation bonds	(7,030)	(7,215)	(7,750)
Interest paid on revenue bonds	(26,979)	(21,264)	(20,483)
Interest paid on commercial paper bonds	(832)		
Interest paid on general obligation bonds	(8,120)	(3,086)	(2,135)
Other interest paid	(54)		
Interest received on invested bond proceeds	1,349	1,374	1,117
Proceeds from sale of capital assets	19,044	8,525	13,084
Ad valorem tax levy receipts	35,531	35,554	35,501
Receipts from federal grants-in-aid	23,398	18,259	17,930
Passenger facility charge receipts	33,664	33,125	32,035
Net cash provided (used) by capital and related financing activities	12,741	25,831	(64,116)
INVESTING ACTIVITIES:			
Purchases of investment securities	(247,317)	(140,608)	(246,009)
Proceeds from maturities of investment securities	133,777	182,231	184,179
Interest received on investments	10,295	9,097	7,345
Investment costs	(129)	(134)	(115)
Net cash provided (used) by investing activities	(103,874)	50,586	(54,600)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	7,371	162,639	(29,274)
CASH AND CASH EQUIVALENTS:			
Beginning of year	282,902	120,263	149,537
End of year	$ 290,273	$ 282,902	$ 120,263

See notes to the financial statements

Years ended December 31, 1998, 1997, and 1996

NOTE 1: ACCOUNTING POLICIES

Organization: The Port of Seattle (the Port) is a municipal corporation organized on September 5, 1911, through enabling legislation by consent of the voters within the Port district. In 1942, the local governments in King County selected the Port to operate the Seattle-Tacoma International Airport (the Airport). The Port is considered a special purpose government with a separately elected commission of five members and is legally separate and fiscally independent of other state or local governments. The Port has no stockholders or equity holders. All revenues or other receipts must be disbursed in accordance with provisions of various statutes and agreements with the holders of its bonds.

The Port is comprised of two operating divisions. The Aviation Division predominately serves the air travel needs of a five-county area, with the largest being King County. The Airport has scheduled passenger service provided by 28 air carriers, including 15 major carriers, three commuter carriers, and ten foreign flag carriers. The Marine Division predominately focuses on containerized cargo. International containerized cargo arriving by ship is transferred to various modes of land transportation destined for other regions of the country. Domestic containerized cargo arriving by various modes of land transportation is transferred to outbound ships for distribution to other countries around the world. The Port is a landlord marine port with major tenants including shipping companies, terminal operators, and other marine-related businesses. Both divisions have labor workforces subject to various collective bargaining agreements. These workforces support the operations and maintenance of the divisions.

Basis of accounting: The Port is accounted for on a flow of economic resources measurement focus. Its financial statements are prepared in accordance with generally accepted accounting principles as applied to governmental units using the accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Port has applied all applicable GASB pronouncements as well as the following pronouncements (unless they conflict with or contradict GASB pronouncements): *Statements and Interpretations of the Financial Accounting Standards Board* (FASB), *Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.* The more significant of the Port's accounting policies are described below.

Use of estimates: The preparation of the Port's financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Significant risks and uncertainties: The Port is subject to certain business risks which could have a material impact on future operations and financial performance. These risks include economic conditions, collective bargaining disputes, Environmental Protection Agency regulations, and federal government regulations.

Landing fees: The cost of airport facilities constructed or acquired with proceeds from revenue bonds are to be recovered under the provisions of a contract with the tenant airlines. The contractual agreement with the airlines provides that they will pay annual charges of the sum of the net cost of operating the airport and a coverage factor of 1.35 times the required debt service on the revenue bonds.

Ad valorem tax revenues: Ad valorem taxes received by the Port are utilized for the acquisition and construction of facilities, for the payment of principal and interest on general obligation bonds which were issued for the acquisition or construction of facilities, or for environmental expenses. The Port includes ad valorem tax revenues and interest on general obligation bonds in the statement of operations.

Passenger facility charges: Passenger facility charges (PFCs) generate revenue to be expended by the Port for eligible projects and the payment of principal and interest on specific revenue bonds as determined by applicable federal legislation. PFC revenues are recorded as nonoperating income in the statements of operations when they are collected by the airlines. During 1998, the Port received approval from the Federal Aviation Administration (FAA) for an additional application. This application funds additional eligible projects and backs $280,000,000 in revenue bonds through December 1, 2023.

Depreciation applicable to assets acquired with passenger facility charge funds is transferred from equity from operations to equity from taxation. Interest income associated with passenger facility charges is also transferred from equity from operations to equity from taxation.

Federal grants-in-aid: The Port receives federal grants in aid funds for construction of airport and marine facilities and other capital activities related to the Airport. Depreciation applicable to assets acquired with grants in aid funds is transferred from equity from operations to equity from grants and donations.

Land, facilities, and equipment: Land, facilities, and equipment are stated at cost, less accumulated depreciation. Costs applicable to noise damage remedies and air rights, together with the cost of litigation, generally are capitalized as a cost of the property. Depreciation is computed on a straight line basis. Buildings and improvements are assigned lives of 30 to 50 years, equipment six to 20 years, and furniture and fixtures five to ten years.

Employee benefits: Eligible Port employees earn paid time off annually, depending on length of service. A stipulated maximum of paid time off and extended illness leave may be accumulated by employees. Terminated employees are entitled to be paid for unused paid time off and, under certain conditions, a portion of unused extended sick leave.

Investments and cash equivalents: It is the Port's intention to hold investments to maturity. All short-term investments with a maturity of three months or less at date of purchase are considered to be cash equivalents. Investments are carried at fair value plus accrued interest. Fair values are determined based on quoted market rates. Gains or losses due to market valuation changes are recognized in the statements of operations.

Environmental reserves: The Port's policy is to accrue amounts for environmental liabilities when they are determined to be probable and reasonably estimable. When the Port's obligation becomes fixed or reliably determinable, the liability is discounted using the Port's cost of capital and the projected periods of cash payments. As of December 31, 1998, there are no liabilities that met the criteria for discounting. Insurance proceeds, if any, are evaluated separately from the Port's liability.

Advanced debt refundings: The accounting gain or loss resulting from advanced debt refundings is deferred and amortized over the remaining life of the old debt, or the life of the new debt, whichever is shorter.

Payments in lieu of taxes: The Port, on behalf of the state of Washington, collects applicable leasehold taxes from its tenants. The taxes are a pass-through to the State, and are therefore not reflected as an expense or revenue by the Port.

New accounting pronouncements:

Investments: In March 1997, the GASB issued Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools.* The statement requires that certain investments be reported on the balance sheet at fair value and the gains and losses on investments be reported in the statement of operations. The provisions of this statement were applied retroactively, and accordingly, the balance sheet for 1997 and the statements of operations, equity, and cash flows for 1997 and 1996 have been restated. The impact of the restatement on the 1997 balance sheet is as follows

	1997 as previously stated	Changes	1997 restated
Cash and cash equivalents restricted for debt service and acquisition of land, facilities, and equipment	$ 225,211	$ 895	$ 226,106
Investments and accrued interest restricted for debt service and acquisition of land, facilities, and equipment	104,584	495	105,079
Cash and cash equivalents, unrestricted	51,447	(158)	51,289
Cash and cash equivalents, restricted	5,507		5,507
Investments	52,055	131	52,186

In addition, the 1997 and 1996 statements of operations, equity, and cash flows were restated to reflect unrealized gains (losses) of $1,584,610 and $(166,000), respectively.

Deferred compensation: The Port offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan is available to all salaried employees of the Port and to wage employees as negotiated. In 1998, the Port placed its Deferred Compensation Plan assets in trust as required under the Small Business Job Protection Act of 1996. The trust requirements were met by establishing a qualifying insurance contract.

In connection with establishing this trust, the Port adopted GASB No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans,* which necessitated the removal of the plan's assets and liabilities from the Port's balance sheet. The effect of the adoption is to reduce the Port's assets and liabilities as of December 31, 1998, by $31,604,518, the fair market value of the plan assets as of December 31, 1997. This statement was not applied retroactively, and therefore, the related assets and liabilities remain on the 1997 balance sheet.

Segment reporting: In June 1997, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 131, *Disclosures about Segments of an Enterprise and Related Information,* which establishes standards for the way that public business enterprises report information about operating segments in annual financial statements. This statement also establishes standards for related disclosures about products and services, geographic areas, and major customers. The Port adopted SFAS No. 131 in 1998 and has provided information on segments in Note 11. The adoption of this standard does not have any impact on the results of operations or financial condition of the Port.

Reclassifications and presentation: Certain reclassifications of prior years' balances have been made to conform with the current year presentation. In addition, the Port changed its method of presenting cash flow information from the direct to the indirect method to be more consistent with others in the industry. Such a change is not considered to be a change in accounting principle.

NOTE 2: LAND, FACILITIES, AND EQUIPMENT

The Port periodically reviews its long-lived assets for impairment and, upon indication that the carrying value of such assets may not be recoverable, recognizes an impairment loss by a charge against current operations.

Land, facilities, and equipment consist of the following at December 31 (in thousands):

	Marine	Aviation	Corporate	Total
1998:				
Land and air rights	$ 405,561	$ 414,169	$ 1,957	$ 821,687
Facilities and improvements	666,244	668,112	37,692	1,372,048
Equipment, furniture, and fixtures	122,680	35,758	53,116	211,554
	1,194,485	1,118,039	92,765	2,405,289
Less accumulated depreciation	244,513	288,384	46,039	578,936
	$ 949,972	$ 829,655	$ 46,726	$1,826,353
1997:				
Land and air rights	$ 385,417	$ 336,073	$ 1,957	$ 723,447
Facilities and improvements	570,293	626,687	37,739	1,234,719
Equipment, furniture, and fixtures	116,912	33,848	49,121	199,881
	1,072,622	996,608	88,817	2,158,047
Less accumulated depreciation	224,134	253,132	41,310	518,576
	$ 848,488	$ 743,476	$ 47,507	$1,639,471

NOTE 3: SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

A reconciliation of cash and cash equivalents reflected in the statement of cash flows to the balance sheet is as follows (in thousands):

	Current assets	Restricted assets	Total
Balance, December 31, 1996	$ 41,033	$ 79,230	$ 120,263
Net increase	10,256	152,383	162,639
Balance, December 31, 1997	51,289	231,613	282,902
Net increase (decrease)	38,625	(31,254)	7,371
Balance, December 31, 1998	$ 89,914	$200,359	$ 290,273

NOTE 4: DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS

The King County Treasurer is the *ex officio* treasurer of the Port of Seattle and, as such, makes investments at the direction of Port management. State investment statutes authorize King County (the County) to invest primarily in certificates of deposit issued by Washington State financial institutions, obligations of the U.S. Treasury, commercial paper (top grade), agencies and instrumentalities, repurchase agreements, and bankers' acceptances issued in the secondary market.

Deposits: Certificates of deposit are held in safekeeping in qualified depositories. Certificates of deposit in excess of the $100,000 Federal Deposit Insurance Corporation (FDIC) insurance limitation are collateralized by the assets of the financial institutions in the State of Washington Public Deposit Protection Commission (PDPC) pool. Deposits are carried at cost plus accrued interest.

Cash and Investments: The County's safekeeping bank, or its New York agent, takes possession of marketable investment securities. Securities used as collateral for repurchase agreements are held by third-party banks, operating under tri-party agreements between King County, the third-party safekeeping bank, and the County's investment brokers. The County's investment policies require that securities underlying repurchase agreements must have a market value of at least 102% of the cost of the repurchase agreement for terms less than 30 days and 105% for terms in excess of 30 days. The County does not invest in repurchase agreements in excess of 60 days. Investments are to be categorized to give an indication of the level of credit risk assumed by the Port. All the Port's investments reside in Category 1, which includes investments that are insured or registered or for which the securities are held in the Port's name or its agent.

Investments consist of the following at December 31:

	1998	1997
Cash	$ 14,648,761	$ 9,085,494
U.S. Treasury bills	7,278,272	5,082,403
U.S. Treasury notes	227,805,869	82,828,005
Tri-party repurchase agreements	109,491,500	149,628,850
Repurchase agreements	14,562,000	50,901,000
Commercial paper	151,571,102	86,780,913
Zero coupon bonds	319,858	22,243,997
	525,677,362	406,550,662
Deferred compensation assets		31,604,518
Accrued interest	2,836,356	1,879,471
Other	148,680	132,590
	$ 528,662,398	$ 440,167,241

NOTE 5: ACCOUNTING FOR LEASES

A significant portion of the marine terminal land, facilities, and equipment is leased to tenants under operating leases. Due to the nature of the contractual agreement with tenant airlines as discussed in Note 1, minimum rentals applicable to airport leases which are accounted for as operating leases are not determinable.

Minimum future rental income on noncancellable operating leases on marine terminal facilities is as follows (in thousands):

Year ending December 31,	
1999	$ 39,558
2000	27,560
2001	25,474
2002	24,181
2003	24,827
Thereafter	708,596
	$ 850,196

In June 1994, the Port executed a sixth amendment to its lease with Eagle Marine Services (a wholly owned subsidiary of American President Lines which handles terminal operations) at Terminal 5. The amendment includes the current lease of 83 acres, adds an additional 75 acres plus an option for an additional 30 acres, and extends the lease to a new 30-year term after completion of a major expansion project of the terminal. This project is expected to be complete in 1999. The above table includes minimum future rental income relating to this amendment in the amount of $730,000,000. Minimum future rental income for the 30-acre option has been excluded. Assumptions used in these calculations are based on the construction and pricing schedules in the sixth amendment in conjunction with estimated Consumer Price Index rates.

Effective December 1996, the Port and Stevedoring Services of America (SSA) entered into a new lease at Terminal 18. The new lease provides for substantial improvements to the existing 110-acre premises as well as a 90-acre expansion. The 30-year term will commence upon total facility completion of the new improvements, currently scheduled for the year 2001. Due to an early termination clause in 1999 relating to land and property rights, necessary permits and railroad access, minimum future rental income included above has been initially defined as the noncancellable portion of the lease through April 30, 1999, which amounts to $2,300,000. The remaining portion of the future rental income on the cancellable portion of the lease (from April 30, 1999, through mid 2030) of approximately $958,000,000, based on Consumer Price Index estimates, has been excluded from the table above.

NOTE 6: LONG-TERM DEBT

The outstanding longterm debt as of December 31, 1998, consists of the following (in thousands):

	Earliest call or year last series matures	Long-term portion	Current maturities
Revenue bonds (by coupon rate):			
3.80% – 5.00%	1998 – 2009	$ 35,250	$ 3,830
3.75 – 5.00	1998 – 2011	25,390	260
4.00 – 4.25	1998		4,535
4.60 – 5.00	1998 – 2000	1,940	2,965
Variable (4.10% at December 31, 1998)	2022	106,390	2,440
4.00 – 5.25	1998 – 2001	13,280	7,760
4.00 – 5.25	1998 – 2012	25,060	1,370
4.00 – 5.375	1998 – 2017	98,470	1,425
5.60 – 6.50	1998 – 2006	31,780	6,500
5.00 – 6.00	1999 – 2017	71,485	3,035
5.10 – 5.375	2000 – 2005	19,985	
5.125 – 6.00	2005 – 2022	120,375	
5.25	2013 – 2017	15,035	
5.375	2018 – 2019	7,220	
5.50	20[illegible]1	31,820	
5.50 – 6.00	1998 – 2001	9,440	3,315
6.00	2012 – 2014	11,595	
6.00	2011 – 2017	37,330	
6.70	2007 – 2010	14,910	
6.70 – 7.10	1998 – 2000	2,825	2,645
7.10 – 7.25	2001	1,243	
7.15 – 7.30	2002	1,951	
7.20 – 7.35	2003	1,806	
7.40	2001 – 2003	11,085	
7.30	2005	10,270	
7.60	2004 – 2009	7,890	
7.70	2011 – 2011	6,525	
Total revenue bonds		720,350	40,080
General obligation bonds (by coupon rate):			
4.70% – 5.90%	1998 – 2011	94,230	5,485
5.75	2012 – 2014	35,370	
Variable (4.00% at December 31, 1998)	2004	11,700	1,900
Total general obligation bonds		141,300	7,385
Passenger facility charges revenue bonds (by coupon rate):			
5.00 – 5.375	2002 – 2016	144,010	
5.00 – 5.50	2016 – 2023	118,490	
Total passenger facility charges revenue bonds		262,500	
Commercial paper (3.10%-3.15% at December 31, 1998)			80,291
Notes payable (8.5%)	1998 – 2001	451	199
Capital appreciation bonds		4,387	
		1,128,988	127,955
Unamortized bond discount, net		(13,791)	
		$ 1,115,197	$ 127,955

The Passenger Facility Charge Revenue Bonds are secured by a first lien pledge of the revenues generated from the Passenger Facility Charges imposed. The remaining revenue bonds are secured by a pledge of gross or net revenues of the Port, payable from funds prior to payment of maintenance and operating costs. The general obligation bonds and interest thereon are payable from ad valorem taxes. Certain revenue bonds are issued at a discount. Discounts on revenue bonds and deferred financing costs are amortized over the life of the related debt, using a method that approximates the effective interest method.

During 1998, the Port issued $73,180,000 of revenue bonds and $27,930,000 in subordinate lien revenue bonds for the purpose of advance refunding $69,735,000 in outstanding long-term debt and $25,145,000 in outstanding long-term subordinate lien debt, respectively. By completing this refunding, the Port in effect reduced its aggregate debt service payments by approximately $9,387,774 and obtained an economic gain (difference between the present value of the old and new debt service payments) of $5,168,154. The accounting loss related to this refunding was $5,891,068 and is being deferred and amortized over the life of the refunding debt.

The Port also issued $262,500,000 in Passenger Facility Charge Revenue Bonds pursuant to a PFC Master Resolution in 1998. These bonds are secured by a pledge of revenues to be received by the Port from certain passenger facility charges imposed by the Port at Seattle-Tacoma International Airport. The proceeds are to be used, among other things, to finance or refinance a portion of the costs of the design and construction of a third runway, the expansion of Concourse A, and the replacement of a passenger conveyance system at the airport.

During 1997, the Port issued $108,830,000 in revenue bonds to finance marine related improvements. These projects will include acquisition of properties in conjunction with the expansion of Terminal 18 and purchase of certain equipment. The Port also issued $140,360,000 in revenue bonds to finance airport-related improvements. These projects include supporting the Acoustical Insulation and Property Acquisition program and the expansion of the public parking terminal.

A resolution of the Port Commission of the Port authorized the sale of Subordinate Lien Revenue Notes (tax-exempt commercial paper), in an aggregate principal amount of not to exceed $100,000,000, for the purpose of financing and refinancing capital improvements within the Port, for working capital, and for paying maturing revenue notes of the same series and/or reimbursing the credit providers for advances made. The Port had outstanding commercial paper of $80,291,000 and $6,605,000 as of December 31, 1998 and 1997, respectively.

During 1996, the Port issued $108,340,000 of revenue bonds for the purpose of financing infrastructure, and environmental, regulatory, and customer service projects at Seattle-Tacoma International Airport.

It is the Port's practice when defeasing bonds to place the proceeds of the new bonds in irrevocable trusts to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the financial statements. As of December 31, 1998, the following amounts are held in trust accounts:

1998 refunding	$ 99,175,000
1994 refunding	$ 24,500,000

During mid to late 1999, it is anticipated that the Port will issue approximately $200,000,000 in revenue bonds and $100,000,000 in general obligation bonds for the aviation and marine divisions, respectively. This is based on the Port's internal capital plan of finance.

The Port monitors for the existence of any rebatable arbitrage interest associated with its tax-exempt debt. The rebate is based on the differential between the interest earnings from the investment of the bond proceeds as compared to the interest expense associated with the respective bonds. As of December 31, 1998, the Port has estimated that an arbitrage rebate in the amount of approximately $103,000 existed in conjunction with its 1993C debt reserve fund and has recognized a liability in this amount. The actual amounts were paid at the required due dates of February 8 and March 4, 1999, to the Internal Revenue Service. Other outstanding bond issues have potential arbitrage rebatable earnings; however, management estimates indicate that no additional potential arbitrage rebate exists as of December 31, 1998.

Interest costs capitalized were $20,921,005 (net of interest income of $14,343,568) in 1998, $21,639,317 (net of interest income of $12,260,322) in 1997, and $15,877,174 (net of interest income of $9,087,302) in 1996.

Aggregate annual payments on long-term debt at December 31, 1998, exclusive of variable interest on $13,600,000 and $108,830,000 of variable general obligation bond principal and subordinate lien revenue bond principal, respectively, are as follows (in thousands):

	Principal	Interest	Total
1999	$ 127,955	$ 56,334	$ 184,289
2000	49,521	54,224	103,745
2001	50,494	53,632	104,126
2002	51,513	52,545	104,058
2003 and thereafter	977,460	486,904	1,464,364
	$ 1,256,943	$ 703,639	$ 1,960,582

The fair value of long-term debt as of December 31, 1998, is $1,307,256,245. The fair value is estimated using quoted market prices.

In December 1997, in anticipation of a future revenue bond issuance by the Port of Seattle or the Industrial Development Corporation of the Port of Seattle (IDC), each entity entered into a forward bond purchase contract with an anticipatory interest rate hedge. These contracts represent a commitment to deliver bonds at a future date. Depending on whether the IDC or the Port ultimately delivers the bonds, the unused forward contract will expire with no associated liability or benefit. Under the surviving contract, the principal amount of bonds to be delivered is set at $150,000,000.

In 1999, the contract was amended, for the Port of Seattle only, to extend the terms of the contract from March 15, 1999 to November 1, 1999. The bonds, however, can be issued at any time during the life of the contract. The contracts protect the Port against increasing interest rates from the date of the contracts until the bonds are issued. There exists a forward premium associated with locking in interest rates on bonds that will be delivered in the future. This forward premium will vary depending on the timing of the bond issuance. In the event that the Port terminates the surviving contract, cash settlement would be required to be made between the Port and the investment bank, which would vary based on the direction and magnitude of changes in interest rates. If this termination were to have occurred on December 31, 1998, the Port would have been obligated to pay approximately $11,622,000.

The Port has not recorded any asset or liability associated with these transactions, as the future potential cash settlement is neither probable nor reasonably estimable, and they provide an effective interest rate hedge.

NOTE 7: PENSION PLANS

Public Employees' Retirement System (PERS): Substantially all of the Port's full-time and qualifying part-time employees, other than those covered under union plans, participate in the PERS. This is a statewide local government retirement system administered by the Department of Retirement Systems, under cost-sharing, multiple-employer public employee retirement systems.

Participants who joined the system by September 30, 1977, are Plan I members. Those joining thereafter are enrolled in Plan II. Retirement benefits are financed from employee and employer contributions and investment earnings. Retirement benefits in both Plan I and Plan II are vested after completion of five years of eligible service.

Plan I members are eligible for retirement after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2% per year of service of the highest compensation during any two consecutive years of service, capped at 60%.

Plan II members may retire at the age of 65 with five years of service, or at 55 with 20 years of service, with an allowance of 2% per year of service of the final average salary, based on the highest compensation during any consecutive five-year period. Plan II retirements prior to 65 are actuarially reduced. There is no cap on years of service credit and a cost of living allowance is granted, capped at 3% annually.

Each biennium, the Washington State Pension Funding Council adopts Plan I employer contribution rates. Employee contribution rates for Plan I were established by statute at 6% and do not vary from year to year. The employer and employee contribution rates for Plan II are set by the director of the Department of Retirement Systems based on recommendations by the Office of the State Actuary to continue to fully fund the plan. All employers are required to contribute at the level established by state law. The Port's covered payroll for PERS for the year ended December 31, 1998, was $38,481,900.

The Port's contribution rates expressed as a percentage of covered payroll as of December 31, 1998, were as follows:

	PERS Plan I required rate	PERS Plan II required rate
Employer	7.32 %*	7.32 %*
Employee	6.00	4.65
	13.32 %	11.97 %

*The employer rates do not include the employer administrative expense fee currently set at 0.18%.

Both the Port and the employees made the required contributions. The Port's required contributions for the year ended December 31, were as follows:

	PERS Plan I	PERS Plan II
1998	$ 805,771	$ 2,011,104
1997	832,006	1,098,813
1996	846,455	1,763,783

The pension obligation was calculated on a pension system basis and cannot be disclosed on a plan basis. PERS does not make separate measurements of assets and pension obligations for individual employers.

Law Enforcement Officers' and Fire Fighters' Retirement System: LEOFF is a cost sharing multiple employer defined benefit pension plan. Membership in the plan includes all full time, fully compensated, local law enforcement officers and fire fighters. LEOFF is comprised solely of nonstate employees. The LEOFF system includes two plans.

Participants who joined the system by September 30, 1977, are Plan I members. Those joining thereafter are enrolled in Plan II. Retirement benefits are financed from employee and employer contributions investment earnings, and state contributions. Retirement benefits in both Plan I and Plan II are vested after completion of five years of eligible service.

Plan I members are eligible to retire with five years of service at age 50. The benefit per year of service is as follows, with a cost-of-living allowance granted, capped at 3% annually:

Term of service	Percent of final average
5 – 10 years	1.0 %
10 – 20 years	1.5
20+ years	2.0

Plan II members are eligible to retire at the age of 50 with 20 years of service or at 55 with five years of service. Retirement benefits prior to age 55 are actuarially reduced. The benefit is 2% of average salary per year of service. The average salary is based on the highest five-year period. There is no cap on years of service credit and a cost-of-living allowance is granted, capped at 3% annually.

Plan I employer and employee contribution rates are established by statute at 6%. State contribution rates for Plan I are set by the Pension Funding Council to fully amortize the total costs of the plan. Employer, employee, and state contribution rates for Plan II are set by the director of the Department of Retirement systems based on recommendations by the Office of the State Actuary to continue to fully fund the plan. All employers are required to contribute at the level required by state law.

The Port's current year covered payroll for LEOFF for the fiscal year ended December 31, 1998, was $7,105,394.

The Port's required contribution rates expressed as a percentage of covered payroll as of December 31, 1998, were:

	LEOFF Plan I	LEOFF Plan II (firefighters)	LEOFF Plan II (police officers)
Employer	6.00 %*	5.09 %*	8.66 %
Employee	6.00	8.48	8.48
	12.00 %	13.57 %	17.14 %

*The employer rates do not include the employer administrative expense fee currently set at 0.18%.

Both the Port and the employees made the required contributions. The Port's required contributions for the years ended December 31 were:

	LEOFF Plan I	LEOFF Plan II (firefighters)	LEOFF Plan II (police officers)
1998	$ 26,229	$ 173,818	$ 281,741
1997	28,008	164,467	274,695
1996	29,129	161,297	222,406

Historical trend information regarding both of these plans is presented in Washington State's Department of Retirement Systems' 1998 annual financial report. A copy of this report may be obtained at:

Department of Retirement Systems
Point Plaza West
1025 East Union Street
P.O. Box 48380
Olympia, Washington 98504-8380

NOTE 8: CONTINGENCIES

The Port is a defendant in various legal actions and claims, including environmental cleanup actions that arise during the normal course of business, some of which may be covered by insurance. Although certain lawsuits and claims are significant in amount, the final dispositions are not determinable and, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of the Port. In some cases, the Port has provided reserves for these matters which, in the opinion of management, are adequate.

Amounts received or receivable under federal grants-in-aid programs are subject to audit and adjustment by the granting agency. Any disallowed claims, including amounts already received, may constitute a liability of the Port. The amount, if any, of expenditures which may be disallowed cannot be determined at this time, although the Port expects such amounts, if any, to be immaterial.

During 1996 and 1997, the Port entered into three agreements to sell real estate related to the Central Waterfront Project involving certain contingencies. In 1998, one of the agreements was closed which relinquished all associated contingencies and resulted in a gain on the sale in the amount of $4,500,000. The two remaining agreements are expected to be closed in 1999 or 2000. At the time the contingencies are cleared, the Port will recognize gains (losses) on the sales. The amount of the gains, if any, are indeterminable at this time.

NOTE 9: COMMITMENTS

As of December 31, 1998, the Port has authorized, or made commitments for, the acquisition and construction of marine terminals and airport facilities as follows (in thousands):

Funds committed:	
Marine terminals	$ 38,488
Airport facilities	183,575
Corporate	4,461
Funds authorized:	
Marine terminals	48,868
Airport facilities	630,412
	$ 905,804

NOTE 10: INDUSTRIAL DEVELOPMENT CORPORATION OF THE PORT OF SEATTLE

The IDC is authorized to facilitate the issuance of taxexempt nonrecourse revenue bonds to finance industrial development within the corporate boundaries of the Port. Revenue bonds issued by the IDC are payable from revenues derived as a result of the industrial development facilities funded by the revenue bonds. The bonds are not a liability or contingent liability of the Port, or a lien on any of its properties or revenues other than industrial facilities for which they are issued. At December 31, 1998, industrial revenue bonds outstanding totalled $26,060,000, which were issued for the purposes of acquiring, constructing, and renovating transshipment and manufacturing facilities.

Under GASB No. 14, The Reporting Entity, the Port of Seattle is financially accountable for the IDC. The outstanding Industrial Revenue Bonds are not recorded in the IDC's financial statements, as they represent conduit debt obligations under GASB Interpretation No. 2. The remaining accounts of the IDC are not material to the financial position or results of operations of the Port.

NOTE 11: INDUSTRY SEGMENT INFORMATION

The Port's operations consist of marine terminals and the airport. Indirect costs have been allocated to marine terminals and the airport using various methods based on estimated hours of work, revenue plus expenses, full-time equivalent units, and other factors.

The Port's major customers individually provided revenues equal to at least 10% of the applicable division's total operating revenues. For the Marine Division the revenues from its major customers accounted for 40%, 36%, and 40% of the total Marine Division's operating revenues in 1998, 1997, and 1996, respectively. For the Aviation Division, the revenues from its major customers accounted for 29%, 28%, and 31% of the total Aviation Division's operating revenues in 1998, 1997, and 1996, respectively.

Operating revenues, as reflected in the statements of operations, from the Port's major customers are as follows (in thousands):

	1998	1997	1996
Marine Division:			
Revenues	$ 35,536	$ 30,664	$ 30,048
Number of major customers	3	3	3
Aviation Division:			
Revenues	$ 45,284	$ 40,092	$ 41,583
Number of major customers	2	2	2
Total revenues of all major customers	$ 80,820	$ 70,756	$ 71,631
Total number of major customers	5	5	5

The Port's operating revenues are derived from various sources. The Marine Division's operating revenues are principally derived from the leasing of marine terminal facilities. The Airport's operating revenues are derived primarily from it airline agreements, concession agreements and other business arrangements.

Operating revenues, as reflected in the statements of operations, from the Port's major sources are as follows (in thousands):

	1998	1997	1996
Marine Division:			
Property rentals	$ 42,663	$ 37,085	$ 36,281
Equipment rental	13,891	14,230	11,605
Distribution and storage	11,088	11,866	12,036
Other	21,064	22,290	15,553
Total Marine Division revenues	$ 88,706	$ 85,471	$ 75,475
Aviation Division:			
Property rentals	$ 74,398	$ 68,962	$ 64,073
Landing fees	35,720	29,768	28,629
Parking	37,374	37,020	35,067
Other	6,843	6,220	6,667
Total Aviation Division revenues	$ 154,335	$ 141,970	$ 134,436

Financial information by segment for the years ended December 31, is as follows (in thousands):

	1998 Marine	1998 Airport	1998 Total
Operating revenues	$ 88,706	$ 154,335	$ 243,041
Operations, maintenance, and environmental expenses	45,524	87,732	133,256
Corporate allocations	8,097	11,795	19,892
Total operating expenses	53,621	99,527	153,148
Net operating income before depreciation	35,085	54,808	89,893
Depreciation	29,892	34,206	64,098
Net operating income, after depreciation	5,193	20,602	25,795
Revenue bond interest expense	(12,761)	(18,713)	(31,474)
Interest income	3,900	7,744	11,644
Other nonoperating income (expense)	3,689	(6,515)	(2,826)
Income (loss) before taxation, passenger facility charges, and general obligation bond interest	21	3,118	3,139
Tax levy	35,515		35,515
General obligation bond interest expense	(8,291)		(8,291)
Passenger facility charges		33,664	33,664
Passenger facility revenue bond interest expense		(89)	(89)
Excess of revenue over expense	$ 27,245	$ 36,693	$ 63,938
Identifiable fixed assets	$ 949,972	$ 829,655	$ 1,779,627
Other identifiable assets	124,109	669,159	793,268
Identifiable assets	$ 1,074,081	$ 1,498,814	2,572,895
Cash, investments, and facilities not identifiable to an industry segment			62,367
			$ 2,635,262
Capital expenditures	$ 135,654	$ 229,267	$ 364,921
Total debt	$ 464,774	$ 778,378	$ 1,243,152

1997 Marine	1997 Airport	1997 Total	1996 Marine	1996 Airport	1996 Total
$ 85,471	$ 141,970	$ 227,441	$ 75,475	$ 134,436	$ 209,911
43,340	77,328	120,668	38,478	72,229	110,707
7,245	11,626	18,871	6,867	11,370	18,237
50,585	88,954	139,539	45,345	83,599	128,944
34,886	53,016	87,902	30,130	50,837	80,967
24,857	29,512	54,369	22,758	28,345	51,103
10,029	23,504	33,533	7,372	22,492	29,864
(8,965)	(16,981)	(25,946)	(7,748)	(17,378)	(25,126)
4,558	5,913	10,471	4,266	4,196	8,462
(3,777)	(1,810)	(5,587)	3,933	(476)	3,457
1,845	10,626	12,471	7,823	8,834	16,657
35,489		35,489	35,445		35,445
(3,270)		(3,270)	(2,116)		(2,116)
	33,125	33,125		32,035	32,035
$ 34,064	$ 43,751	$ 77,815	$ 41,152	$ 40,869	$ 82,021
$ 848,488	$ 743,476	$ 1,591,964	$ 652,316	$ 711,460	$ 1,363,776
173,826	415,680	589,506	252,555	239,732	492,287
$ 1,022,314	$ 1,159,156	2,181,470	$ 904,871	$ 951,192	1,856,063
		81,082			72,656
		$ 2,262,552			$ 1,928,719
$ 152,492	$ 109,153	$ 261,645	$ 149,901	$ 57,496	$ 207,397
$ 440,581	$ 494,334	$ 934,915	$ 340,401	$ 375,532	$ 715,933

Required Supplementary Information
(unaudited)

December 31, 1998

YEAR 2000 ISSUES (unaudited)

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely affect the Port's operations as early as fiscal year 1999.

Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot ensure that the Port is or will be year 2000 ready, that the Port's remediation efforts will be successful in whole or in part, or that parties with whom the Port does business will be year 2000 ready.

The Port's management is utilizing resources and techniques to mitigate the impacts of year 2000 issues. Leaders have been assigned responsibility for mitigation of the each of the operating divisions and also for the corporate services groups. The Port's stages of readiness are defined below for each of these three groups.

Aviation Division:

In 1998 the Aviation Division of the Port of Seattle identified 127 financial and operating data processing systems and embedded systems with microchips to check for year 2000 compliance. The progress for the Aviation Division is as follows:

Year 2000 work phase	Current status as of March 19, 1999	Projected completion date
Assessment	127/127	Completed August 1998
Remediation (now undergoing repair and replacement)	37/127	October 1999
Validation and testing	17/127	October 1999
Completed systems (year 2000 compliant)	62/127	October 1999

Risks of year 2000 issues: The Aviation Division is analyzing, monitoring and mitigating its year 2000 risks by ensuring that its critical information and operating systems are compliant before January 1, 2000. Additionally, the division is preparing for risks that may occur on January 1, 2000, and throughout the next two quarters. These year 2000 risks include possible failures in its own systems and from organizations that provide critical products and services.

Risks to airport systems: During the assessment phase, airport leaders assigned priorities to each system: safety critical, mission critical (needed for the airport to operate) and non-mission critical. Safety critical and mission critical systems receive top priority for compliance. Currently, 43 of 79 safety and mission critical systems and 19 of 48 non-mission critical systems are year 2000 compliant.

The Aviation Division year 2000 project is on schedule and it is anticipated that all systems will be compliant by October 1999. Nevertheless, the division is simultaneously documenting a contingency plan for each system.

Risks from external factors: Senior airport managers have reviewed potential external risks to the airport tied to the millennium rollover. They identified three worst-case scenarios that could materially affect airport operations and/or revenues if they continued for several days:

- Airlines cannot fly
- Airplane fuel shortages
- Interruptions in utility service: electricity, natural gas and telecommunications

Contingency plans: To reduce these risks, the division has been sharing information, methodology and findings with its aviation partners — and will involve them in future year 2000 contingency plans. The division will survey airlines at least quarterly to determine the year 2000 readiness of their financial systems to avoid interruptions in their payment of landing fees and passenger facility charges. The division is also increasing its access to reserves of airplane fuel, targeting back-up electric generators for safety and mission critical systems and building redundancies within communications. Finally, the division is surveying other key customers, tenants and suppliers quarterly to determine their year 2000 readiness.

The contingency plan, now under development, is scheduled to be complete by June 30, 1999.

Costs to address year 2000 issues:

Historical and future estimated costs of remediation	$ 6,059,919
Historical and future estimated costs for replacement of noncompliant systems	3,302,259
Total Aviation Division year 2000 projected costs	$ 9,362,178**

** Figures do not include any potential costs for future litigation or compliance costs for corporate systems. Costs incurred during the assessment phase are not separately identified above. A portion of these costs are included as costs of remediation. The remainder are not specifically quantifiable and are not considered to be significant by management.

Marine Division:

The Marine Division of the Port of Seattle has so far identified 104 financial and operating data processing systems and embedded systems with microchips to check for year 2000 compliance. The progress for the Marine Division is as follows:

Year 2000 work phase	Current status as of March 10, 1999	Projected completion date
Assessment	104/104	Completed March 1999
Remediation (now undergoing repair and replacement)	3/104	October 1999
Validation and testing	94/104	October 1999
Completed systems (year 2000 compliant)	7/104	October 1999

Risks of year 2000 issues: Within the Marine Division's contingency planning, the year 2000 risks will be analyzed by responding to two areas of focus:

- Bringing the critical systems into compliance before January 1, 2000
- Preparing for risks on January 1, 2000, and throughout the quarter following this date. These year 2000 risks include possible failures in their own systems and in organizations that provide them critical products and services

Risks to marine systems: During the assessment phase, marine leaders assigned priorities to each system: safety critical, mission critical (needed for marine lines of business to operate) and non-mission critical. Safety critical and mission critical systems will receive top priority for compliance.

It is projected that all marine systems will be compliant by October 1999. Simultaneously, a contingency plan is being documented for each system. If a system's remediation falls behind schedule or if an unexpected year 2000 failure occurs at any point, back-up plans will be immediately activated by the division, so that neither safety nor operations are compromised.

Risks from external factors: Senior marine managers have reviewed potential external risks to the lines of business tied to the millennium rollover. The division will be surveying its major customers and key suppliers to determine their year 2000 readiness. The most likely worst case scenario for possible failures will be developed from the surveys and with input from marine leaders. Contingency plans will be created to minimize the potential negative impacts.

The greatest concern is with possible long-term interruptions in electrical power, natural gas or telecommunications services. Consequently, existing emergency plans are being reviewed and augmented to make sure mission critical services can be delivered during an electrical outage.

Contingency plans: The Marine Division's contingency plan is iterative. The risk plan for the division's systems will be activated on June 1, 1999. By September 1, 1999, it is expected that a plan will be published for all other risks occurring between late December 1999 through the first two quarters of 2000. As more is learned about the risks of the division's program and other organizations, the plan will be continually revised and updated to minimize any potential safety, operational and financial impacts.

Finally, the division has and will continue to support sharing of year 2000 information and methodology with its marine partners: other ports, the US Coast Guard, major customers, suppliers, vendors, utilities, and regulatory agencies.

Costs to address year 2000 issues:

Historical and future estimated costs of remediation	$ 850,000
Replacement capital costs of noncompliant systems	150,000
Total Marine Division year 2000 projected costs	$ 1,000,000**

** Figures do not include any potential costs for future litigation. Costs incurred during the assessment phase are not separately identified above. A portion of these costs are included as costs of remediation. The remainder are not specifically quantifiable and are not considered to be significant by management.

Corporate professional and technical services groups:

In 1994, the Port of Seattle Information Technology Department embarked upon a new hardware and software strategy. The Port began replacing its network of mini-computers and terminals with newer server and desktop technology. In addition, all of the Port's major business systems were to be replaced or migrated to the new hardware technology. In the process, the Port replaced non-year 2000 compliant computers and systems with compliant hardware and software.

The Port's main computer network now consists of 11 servers, 23 network servers, and approximately 1200 desktop personal computers, Pentium 133 or better.

New financial systems were implemented in July 1997 for General Ledger, Accounts Payable, Purchasing, Projects, and Budgets. New Accounts Receivable and Billing systems are scheduled for implementation in May 1999 and a new Asset Management system in July 1999. New Human Resources, Benefits Administration, and Payroll systems were implemented in January 1999. The Port's new financial and human resource systems carry a four-digit year for all processing. However, all business systems, including these new financial and human resources systems will be year 2000 tested by the Port in the coming year.

In February 1999, the Port of Seattle Corporate Professional & Technical Services Groups initiated a formal year 2000 Program Office. It is now in the process of finalizing its inventory and assessment of all corporate business systems and the Port's computer network. It has so far identified a combination of 54 business systems, utility software systems, and hardware components to check for year 2000 compliance. The progress of the Corporate Professional & Technical Services Groups is as follows:

Year 2000 work phase	Current status as of March 10, 1999	Projected completion date
Assessment	20/54	May 1999
Remediation (repair and replacement)	1/2	October 1999
Validation and testing	0/54	October 1999
Completed systems (year 2000 compliant)	0/54	October 1999

Risks of year 2000 issues: Within the Corporate Professional & Technical Service Group's contingency planning, the year 2000 risks will be analyzed by responding to two areas of focus:

- Bringing the critical systems into compliance before January 1, 2000
- Preparing for risks on January 1, 2000, and throughout the quarter following this date. These year 2000 risks include possible failures in their own systems and in organizations that provide them critical products and services

Risks to corporate systems: During the assessment phase, Corporate Professional & Technical leaders will assess risk and assign priorities to each system: safety critical, mission critical (needed for corporate business processes to operate) and non-mission critical. Safety critical and mission critical systems will receive top priority for compliance.

Though the Corporate Professional & Technical Services Groups project that all systems will be compliant by October 1999, they are simultaneously documenting a contingency plan for each system should a system's remediation fall behind schedule or should unexpected year 2000 failure occur at any point.

Risks from external factors: Corporate Professional & Technical leaders will review potential external risks to their business processes tied to the millennium rollover. The leaders will survey major vendors, key suppliers, and financial organizations with which the Corporate Professional & Technical Services Groups interface to determine their year 2000 readiness. The most likely worst case scenario for possible failures will be developed from the surveys and with input from corporate leaders. A contingency plan will be created to minimize the potential negative impacts.

The greatest concerns so far are possible long-term interruptions in electrical power and telecommunications services caused by year 2000 problems. Consequently, the Corporate Professional & Technical Services Groups will incorporate into the contingency plan an assessment of the level of service that can be delivered for corporate mission critical business systems during electrical outage or brownout conditions.

Contingency plan: The year 2000 contingency plan for the Corporate Professional & Technical Services Groups is iterative. It is projected that the contingency plan for corporate systems will be ready October 1999. As more is learned about the risks of the systems and other organizations, this plan will be continually revised and updated to minimize any potential safety, operational and financial impacts.

Finally, support in sharing of year 2000 information and methodology will continue with other ports, major customers, suppliers, vendors, utilities, and regulatory agencies.

Costs to address year 2000 issues:

Historical and future estimated expense costs of remediation	$ 700,000
Replacement capital costs of noncompliant systems	1,450,000
Total Corporate Professional & Technical Services year 2000 projected costs	$ 2,150,000**

** Figures do not include any potential costs for future litigation. Costs incurred during the assessments phase are not separately identified above. A portion of these costs are included as costs of remediation. The remainder are not specifically quantifiable and are not considered to be significant by management.

Financial and Operational Highlights

The Port of Seattle is principally engaged in developing and managing commerce through the Seattle Harbor and Seattle-Tacoma International Airport. The Port provides freight and passenger terminals, and storage and transfer facilities for different modes of transportation, improves land for sale or lease for industrial or commercial purposes and creates industrial development districts. The Port is comprised of two operating divisions, Marine and Aviation, and a number of Professional and Technical Services Departments, which provide support services to the operating divisions.

Business Environment

Seattle-Tacoma International Airport is the sole commercial airport serving the Seattle metropolitan area. Although approximately 70 percent of the passengers using the airport either begin or end their air travel in the Seattle area, the airport competes with other West Coast airports for direct international air service. Principal competitive factors for the airport include charges assessed to the airlines, efficiency of airport design, gate availability and duration and frequency of air traffic delays.

Although the Port of Seattle provides a variety of maritime-related services, the Marine Division's principal business focus and largest revenue source is container shipping, with the Port serving as one of the major West Coast gateways for the growing trade between the United States and the Pacific Rim. Between 70 percent and 80 percent of the container volume from Asia through Seattle is destined to the interior of North America, and about 25 percent of Seattle's container exports to Asia originate in the interior of North America. Because such cargo can be shipped through any major West Coast port, this market is highly competitive. Major factors influencing shipping lines' routing decisions include relative sailing time, port pricing, terminal efficiency and quality and price of truck and rail connections. Since the Port of Seattle operates primarily as a landlord port through the provision of leased facilities and rental of equipment, maritime revenues are somewhat insulated from short-term cargo fluctuations.

For a more detailed discussion of the Port's preparations to mitigate the Year 2000 impacts, see the Unaudited Required Supplementary Information starting on page 40. The Year 2000 issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely affect the Port's operations as early as fiscal year 1999. The Port's management is utilizing resources and techniques to mitigate the impacts of Year 2000 issues.

Results of Operations

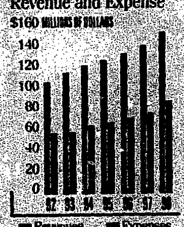
Aviation

Airport operating revenues are determined by formula as the sum of operations, maintenance and environmental expenses and corporate allocations plus 135 percent of airport debt service. Airline landing fees are established annually on a residual basis to cover the difference between lease, concession and other non-airline revenues and the airport's total revenue requirement.

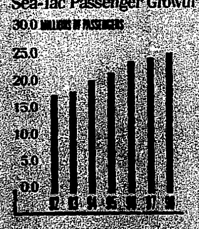
Revenue and Expense

Aviation operating revenue increased by 8.7 percent over that in 1997 as a result of increases in expenses, as per the residual formula. Increases in non-airline revenues helped offset increases in airline landing fees. Total Aviation operations, maintenance and environmental expenses increased 13.5 percent over those in 1997. The increase relates to an overall strategy of improving customer service

Aviation Operating Revenue and Expense



Sea-Tac Passenger Growth



and accommodating growing capacity demands. Significant increases occurred in maintenance and police, and the Port established a new department to focus on airport infrastructure systems. Additionally, the Aviation Division devoted resources to assessing and fixing Year 2000 systems problems. A change in the Port's paid leave program resulted in a large non-recurring reserve expense.

Sea-Tac Passenger Growth

Passenger volume at Sea-Tac in 1998 increased by 4.6 percent over that in 1997. Domestic traffic was up 3.5%, and international traffic increased 16.8%.

Aviation Operations, Maintenance and Environmental Expense Per Enplanement

Operations, maintenance and environmental expense (discussed above) rose faster than the growth in enplanements, resulting in an increase of 8.8 percent in aviation operations, maintenance and environmental expense per enplanement over those in 1997.

Non-Airline Revenue Per Enplanement

Non-airline revenues include concession, parking and other fees not charged directly to the airlines. These revenues help offset the residual landing fee requirement, and thus reduce airline operating costs. Non-airline revenue increased 3.5 percent over that in 1997 due to increases in concession revenue. Non-airline revenue per enplanement decreased 0.7 percent compared to that in 1997 due to enplanements increasing faster than revenues.

Airline Cost Per Enplanement

Airline cost per enplanement reflects the overall airport cost to the airlines for each passenger enplaned. The 1998 cost of $5.20 is 11.6 percent above that in 1997 due to expenses increasing faster than enplanements.

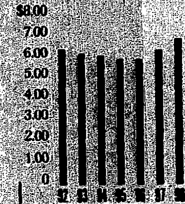
Air Freight

Overall air freight tonnage, exclusive of U.S. mail, increased 4.6 percent compared to that in 1997. Domestic air freight was up 6.3 percent, while international air freight decreased 0.2 percent. Total air cargo, including U.S. mail, was up 8.8% in 1998 over that in 1997.

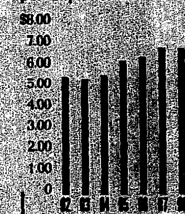
Top Ten Aviation Customers By Revenue

1. Alaska Airlines, Inc.
2. United Airlines, Inc.
3. Northwest Airlines, Inc.
4. Host Marriott Corporation
5. Delta Air Lines, Inc.
6. American Airlines, Inc.
7. Southwest Airlines Co.
8. Horizon Air Industries, Inc.
9. The Hertz Corporation
10. Avis Rent-A-Car System, Inc.

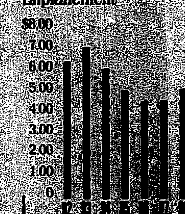
Aviation Operations, Maintenance and Environmental Expense per Enplanement



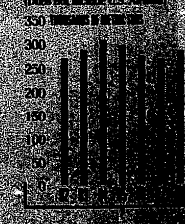
Non-Airline Revenue per Enplanement



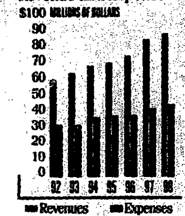
Airline Cost per Enplanement



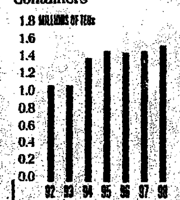
Air Freight
(Does not include U.S. Airmail)



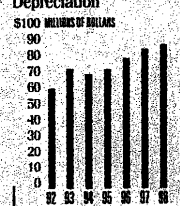
Marine Operating Revenue and Expense



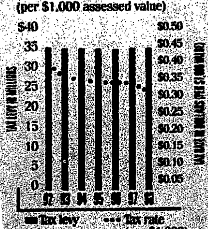
Seattle Harbor Containers



Total Port Net Operating Income Before Depreciation



Tax Levy and Tax Rate (per $1,000 assessed value)



Marine

Revenue and Expense

1998 Marine operating revenues increased 3.8 percent compared to those in 1997. This was largely the result of increased container acreage and crane rentals and better-than-expected revenues generated by Bell Harbor International Conference Center. Total operations, maintenance and environmental expenses increased 5.0 percent compared to those in 1997. Normalizing for environmental expense reserve reductions in 1998 and 1997, operations, maintenance and environmental expenses in 1998 remained essentially flat.

Seattle Harbor Containers

Seattle Harbor facilities handled a record volume of container traffic measured in 20-foot Equivalent Units (TEUs) in 1998 of 1.54 million TEUs, up 4.6 percent from those in 1997. International TEUs increased 5.8%, while domestic TEUs decreased slightly.

Top Ten Marine Customers By Revenue

1. APL Ltd.
2. Hasbro, Inc.
3. Stevedoring Services of America
4. Hanjin Shipping Co. Ltd.
5. Trans Pacific Container Service Corporation
6. Matson Navigation Company
7. Distribution & Auto Service, Inc.
8. Cargill Incorporated
9. NYK Line (North America), Inc.
10. Container-Care International, Inc.

Total Port

Net Operating Income Before Depreciation

Due to the Airport and Marine operating results outlined earlier, total Port net operating income before depreciation for 1998 was $89.9 million, an increase of 2.3 percent over that in 1997.

Tax Levy

The Port's tax levy is used for certain harbor-related capital improvements, select environmental expenses and the payment of general obligation debt service. The budgeted levy has remained flat since 1992. Since 1990 the tax levy millage rate assessed King County property owners has decreased by 42 percent.

Staffing

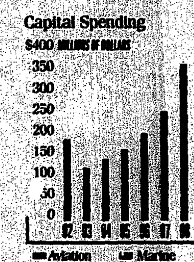
In 1998, the Port had 1,375.2 full-time equivalent positions (FTEs), an increase of 4.9 percent compared to 1997. This increase is due to heightened service demands and to several major capital projects.

Corporate Allocations

Corporate allocations increased 5.4 percent from those in 1997 due to Year 2000 system expenses, outside legal expenses for the Endangered Species Act and public relations expenses for the airport. Corporate allocations as a percent of total operating expense dropped from 13.5 percent in 1997 to 13.0 percent in 1998.

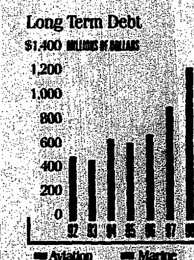
Capital Spending

The Port spent an unprecedented $364.9 million on capital projects in 1998. The Marine Division's $135.7 million of spending on major capital projects included the completion of the Southwest Harbor Project Terminal 5 expansion, property acquisition and improvements for expansion at Terminal 18, berth and electrical system replacement at Terminal 91 and construction of the World Trade Center component of the Central Waterfront Project. At Seattle-Tacoma International Airport, the Port spent $229.3 million on major projects including design, property acquisition and construction for the third runway, ongoing noise mitigation and safety area improvements, improvements to the public parking lot and construction of an employee parking lot.



Economic Impacts

An economic impact study completed in 1994 found that 26,000 jobs in the region depend on the seaport and airport, and that an additional 64,000 visitor industry jobs rely on Seattle-Tacoma International Airport. These jobs, in turn, support 27,000 additional jobs in the community. The study also shows that $475 million in state and local taxes is generated from the $7.5 billion in business revenue that results from Port activities. Based on model assumptions from 1994, increased activity at both the airport and the seaport has likely increased the Port's economic impact on the region.



Debt Information

Long Term Debt

The Port's total debt increased 33.0 percent in 1998, due primarily to the issuance of $262.5 million of Revenue Bonds secured by passenger facility charges and $87.2 million of Subordinate Lien Revenue Notes (Commercial Paper), authorized in 1997.

Debt Service Coverage Ratio — Parity Lien Revenue Bonds

The Port's Parity Lien debt service coverage ratio in 1998 was 1.96.

Revenue Bond Debt Service

The Port's total debt service for revenue bonds secured by operating revenues was $70.5 million in 1998, and will equal approximately $80.9 million in 1999. The Port's total debt service for revenue bonds secured by passenger facility charges revenue was $5.6 million in 1998, and will equal approximately $13.5 million in 1999.

Current Bond Ratings

	Fitch	Moody's	S&P
General Obligation Bonds	—	Aa1	AA+
G.O. Variable Rate [1]	—	P-1/Aa3	A-1+/AA-
Revenue Bonds & Notes:			
Parity Lien	AA	Aa3	AA-
Fixed Rate Subordinate Lien (insured)	AAA	Aaa	AAA
Variable Rate Subordinate Lien [2]	—	VMIG1/Aa3	A-1+/AA-
Subordinate Lien Revenue Notes [3]	—	P-1/Aa3	A-1+/AA-
Passenger Facility Charge (insured)	AAA	Aaa	AAA

(1) Secured by standby letter of credit issued by Bank of America Trust & Savings Association, d/b/a Seafirst Bank

(2) Secured by a direct pay letter of credit issued by Canadian Imperial Bank of Commerce

(3) Commercial Paper secured by a direct pay letter of credit issued by Bank of America National Trust & Savings Association, d/b/a Seafirst Bank

Port Commission
Jack Block
Patricia Davis
Gary Grant
Paige Miller
Clare Nordquist

Executive Office
M. R. Dinsmore, Executive Director

Corporate Staff
Thomas Tierney,
Chief Administrative Officer/
Chief Financial Officer

Linda Strout, General Counsel

Yvonne Tate, Director,
People Programs

Jane L. Kilburn, Director,
Public Affairs

Aviation Division
Gina Marie Lindsey,
Managing Director

Marine Division
Stephen Sewell, Managing Director

General Port Information:
(206) 728-3000
www.portseattle.org

Seattle Marketing and Sales

Marine Division
P.O. Box 1209
Seattle, Washington 98111, U.S.A.
(206) 728-3846
Fax (206) 728-3280
www.portseattle.org

John Pilcher, Director, Marine
Professional & Technical Services
(206) 728-3768
e-mail address: pilcher.j@
portseattle.org

Michael Matthews, Manager,
Container Marketing &
Customer Service
(206) 728-3873
e-mail address: matthews.m@
portseattle.org

Kent Christopher, Customer
Service Representative, Container
Line of Business
(206 728-3569
e-mail address: christopherk@
portseattle.org

Tino Salud, Customer Service
Representative, Central
Waterfront Piers & Properties;
Fishermen's Terminal Piers &
Properties; Shilshole Bay Marina
(206) 728-3139
e-mail address: salud.t@
portseattle.org

Stephen Sasala, Customer Service
Representative, Cargo Piers &
Industrial Properties
(206) 728-3667
e-mail address: sasala.s@
portseattle.org

Marine Division
Market Research
Robert Hannus, Senior Market
Research Analyst
(206) 728-3269
e-mail address: hannus.b@
portseattle.org

Schoeb Ismail,
Market Research Analyst
(206) 728-3282
e-mail address: ismail.s@
portseattle.org

Aviation Division
Seattle-Tacoma
International Airport
P.O. Box 68727
Seattle, Washington 98168, U.S.A.
(206) 248-6862
Telex 703433 PORT SEA UD
Fax (206) 248-6855

Aviation Marketing
Dave Witt, Director
(206) 433-4698
e-mail address: witt.d@
portseattle.org

Kazue Ishiwata, Manager,
Market Development
(206) 248-6857
e-mail address: ishiwata.k@
portseattle.org

International
Don Lorentz, Director, Economic
& Trade Development
(206) 728-3402
e-mail address: lorentz.d@
portseattle.org

S. Kenneth Pai, Director,
International Marketing
(206) 728-3283
e-mail address: pai.k@
portseattle.org

Regional Sales

Inland Northwest
Howard Granger,
Senior Representative,
Trade & Economic Development
801 West Riverside, Suite 302
Spokane, WA 99201
Phone (509) 838-8766
Fax (509) 624-3759
e-mail address: granger.h@
portseattle.org

Asia
Oshu Go, Director, Asia
Room 206, Kokusai Building
3-1-1 Marunouchi
Chiyoda-Ku Tokyo 100-0005, Japan
Phone 81-3-3214-5578
Fax 81-3-3285-0770
e-mail address: oshupos@gol.com

Benjamin P. Wong,
Representative, Hong Kong
P.O. Box 2534
G.P.O. Hong Kong
Phone (852) 2849-8202
Fax (852) 2849-8810
e-mail address: wongckf@
netvigator.com

Kang-Hyuck Song,
Representative, Korea
2/F, Town Building, No. 448-25
Seokyo-Dong, Mapo-Ku
Seoul, Korea
Phone (82-2) 3143-0143/5
Fax (82-2) 325-9115/6

Zheng, Haitang, Representative,
People's Republic of China
Lucky Tower, Room 1603
3, Dong San Huan Bei Road
Cho Yang District
Beijing 100027
People's Republic of China
Phone (86-10) 6467-9166
Fax (86-10) 6467-9166
e-mail address: posbjg@public.
east.cn.net

Kirpa Ram Vij, Representative,
Southeast Asia
171 Chin Swee Road
#09-01 San Centre
Singapore 169877
Phone (65) 538-3988
Fax (65) 538-3386

Writer:
Imbert Matthee,
Media Officer, Port of Seattle

Editor:
Mayo Ochiltree, Port of Seattle

Design:
Marty Roselius Design,
Yvonne San Luis, Designer

Print Production Manager:
Marilyn Farrell, Fontarrell's, Inc.

Photography:
Don Wilson, Tom McCarthy,
Charles Krebs, Tim Heneghan,
Kent Knudson

Port of Seattle
P.O. Box 1209
Seattle, WA 98111
U.S.A.

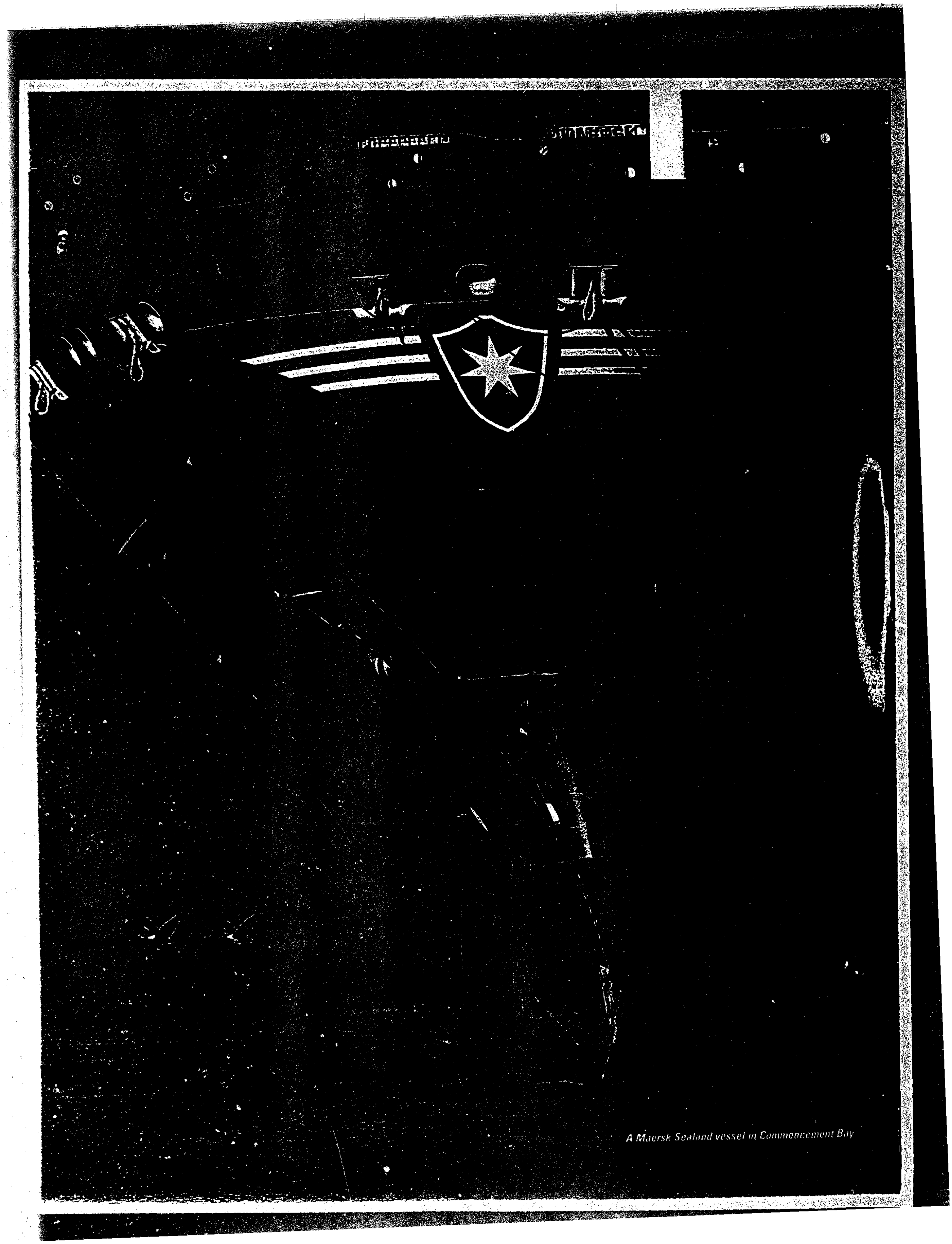
ATTACHMENT No. 2

(Port of Tacoma Annual Report)

Port of Tacoma

Annual Report

1999



A Maersk Sealand vessel in Commencement Bay

results

The Port of Tacoma is known as a pragmatic, results-oriented operation. We lived up to that reputation in 1999 by achieving tangible goals that delivered growth for our customers, improvements to our transportation infrastructure and economic opportunity for our community.

Through our Vision 2020 effort, we also took steps to ensure our long-term ability to produce results. We took a hard look at our land and facilities and identified strategies to maximize our assets.

All of the Port's major container shipping customers implemented or announced plans to expand Tacoma operations in 1999, and we handled a record 1.27 million container TEUs (twenty-foot equivalent units), an increase of nearly 10 percent over 1998.

By having land available when needed and ensuring that waterways, roadways and rail facilities have adequate capacity, we will offer shipping lines and industrial customers a competitive business environment that encourages growth.

That's our pledge to our customers and to our community. It's a pledge that the Port Commission and Staff will work continuously to fulfill.

Sincerely,

R. Ted Bottiger
President, Port of Tacoma Commission

The Port of Tacoma Commission

The five-member Port of Tacoma Commission is the governing body of the Port of Tacoma. The Commission sets policy and authorizes major expenditures.

The Commission appoints an Executive Director, who is responsible for the executive leadership of the Port. Commissioners are elected to four-year terms by voters in Pierce County, Washington. The Commission holds regular public meetings on the first and third Thursdays of each month at the World Trade Center, 3600 Port of Tacoma Road.

Andrea Riniker, *Executive Director*

Andrea Riniker was named Executive Director of the Port of Tacoma in 1997. Prior to joining the Port of Tacoma, she spent five years as Deputy Executive Director of the Port of Seattle. Ms. Riniker has also been Director of Seattle-Tacoma International Airport, Director of the Washington State Department of Ecology, City Manager for the City of Bellevue, Washington, and Assistant City Manager in Austin, Texas. She holds a bachelor's degree in History from the University of Delaware and did graduate work in Urban Studies at the University of Michigan.

Clare Petrich

Ms. Petrich was elected to the Port Commission in November 1995 and took office in January 1996. She graduated from Manhattanville College, Purchase, New York, and earned an M.Ed. from the University of Virginia. Before she began managing Petrich Marine Dock, a marina and manufacturing facility on Tacoma's Thea Foss Waterway, Ms. Petrich lived for several years in Africa and Asia. She is a co-founder of the Commencement Bay Maritime Fest and President of the Board of Directors of the World Trade Center Tacoma. She serves on the Board of the Washington Council on International Trade, the Tacoma-Pierce County Visitor and Convention Bureau, The World Affairs Council – Tacoma, The Tacoma Rescue Mission and The Advisory Council, Catholic Community Services.

Connie Bacon

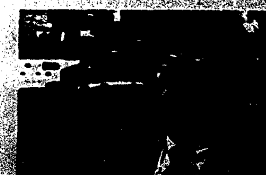
Ms. Bacon was elected to the Commission in 1997 and began her term in 1998. She graduated from Syracuse University and received a Master's Degree in Public Administration from The Evergreen State College. Ms. Bacon was Executive Director of the World Trade Center Tacoma from 1992 to 1997 and served eight years as Special Assistant to Washington State Governor Booth Gardner. Ms. Bacon also worked as Corporate Director of Public Relations for Consolidated Hospitals in Tacoma and has owned and operated her own business. Ms. Bacon is an experienced contributor on China Trade. She is on the Board of Directors of the Washington State China Relations Council, the Tacoma-Pierce County Chamber of Commerce, the Tacoma Art Museum, Camp Brotherhood (Seattle), Tacoma International District Advisory Committee, International Services Development Zone Committee, Pacific Lutheran University (PLU) Business School Advisory Committee, and the South Sound China Relations Council at PLU.

Jack Fabulich

Mr. Fabulich was first elected to the Port Commission in 1977. He served in the U.S. Navy and graduated from the University of Puget Sound (UPS) with a bachelor of arts degree in economics and business. He served 12 years as president of the Parker Paint Manufacturing Company of Tacoma. He is also a member of the Economic Development Board for Tacoma-Pierce County and the Executive Board of the Puget Sound Regional Council. He is a member of the Board of Directors of Columbia Bank, Tacoma Elks and the Tacoma Chapter of the Propeller Club of the United States. Mr. Fabulich is also on the Board of the Washington Public Ports Association. He is a 1998 recipient of the UPS National Alumni Achievement Award.

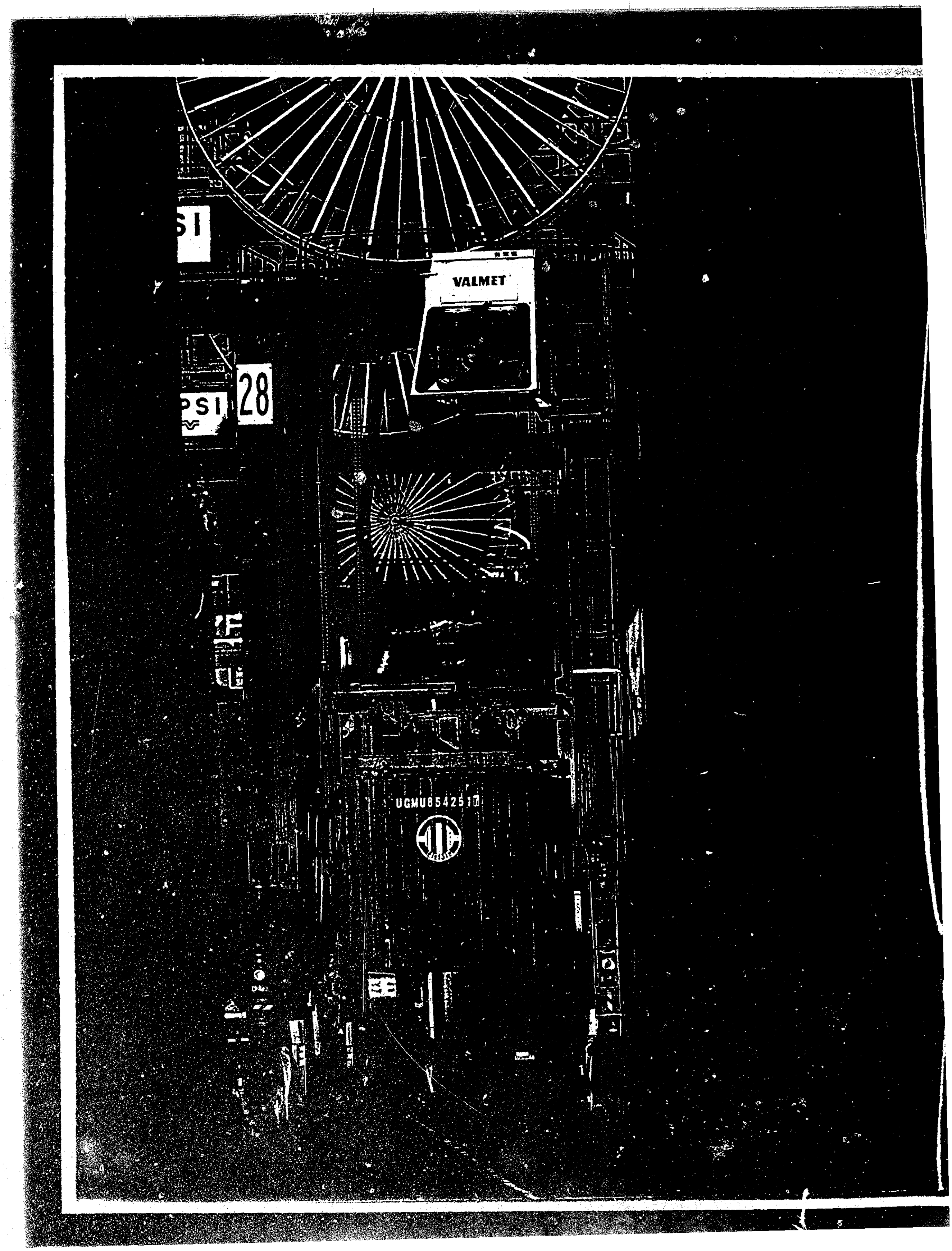
Richard P. Marzano

Mr. Marzano, a Tacoma Longshoreman for 33 years, was elected to the Port Commission in November 1995. He served as president of the International Longshore and Warehouse Union Local 23 from 1989-95. He is a member of the Tacoma Chapter of the Propeller Club of the United States and serves on the Board of Directors of the Hospitality Kitchen at St. Leo's Catholic Church and of the Foss Waterway Development Authority.



R. Ted Bottiger

Mr. Bottiger was appointed to the Port Commission in March 1997 and subsequently elected to the Commission in November 1997. He graduate from the University of Puget Sound in 1956 with a degree in public administration, and from the University of Washington School of Law in 1960. He served four years as an Assistant Attorney General in the Washington State Attorney General's Office and spent 23 years in private legal practice. He served 23 years in the Washington State House of Representatives and Senate, including five years as Senate Majority Leader. In 1987, he was appointed to the Northwest Power Planning Council by former Washington Governor Booth Gardner, and served on the board until his retirement in 1995. Mr. Bottiger sits on the Governor's Blue Ribbon Commission on Transportation. He also serves as a Volunteer Supervisor for the Pierce County Conservation District.


SI
VALMET
PSI
28
UGMU854251

Tacoma delivers, with land, facilities to help container companies grow.

Since its emergence as a major container port in 1985, one of Tacoma's greatest assets has been room to grow. The convergence of deep water and affordable real estate in close proximity to highways and railroads makes Tacoma the right business location for growing container lines.

The changes sweeping the container shipping industry – alliances, consolidations, and the introduction of larger and larger ships – have made Tacoma's physical assets more valuable than ever. And the Port has worked closely with customers to use these assets to anticipate and respond to the advancing tide of change.

The Port is investing nearly $40 million to meet the growth needs of existing container customers. Every one of those customers announced or implemented plans for expansion in Tacoma in 1999.

The Port completed the largest terminal construction project in its history when Hyundai Merchant Marine opened a 60-acre, $100 million container facility in May. Hyundai has already asked the Port to add 20 acres to its terminal and increase the size of its intermodal yard.

The Port also began construction on a 35-acre addition to Evergreen Line's container terminal, which will bring the facility to 75 acres.

"K" Line, another long-time Port customer, added larger ships on its Tacoma service in 1999.

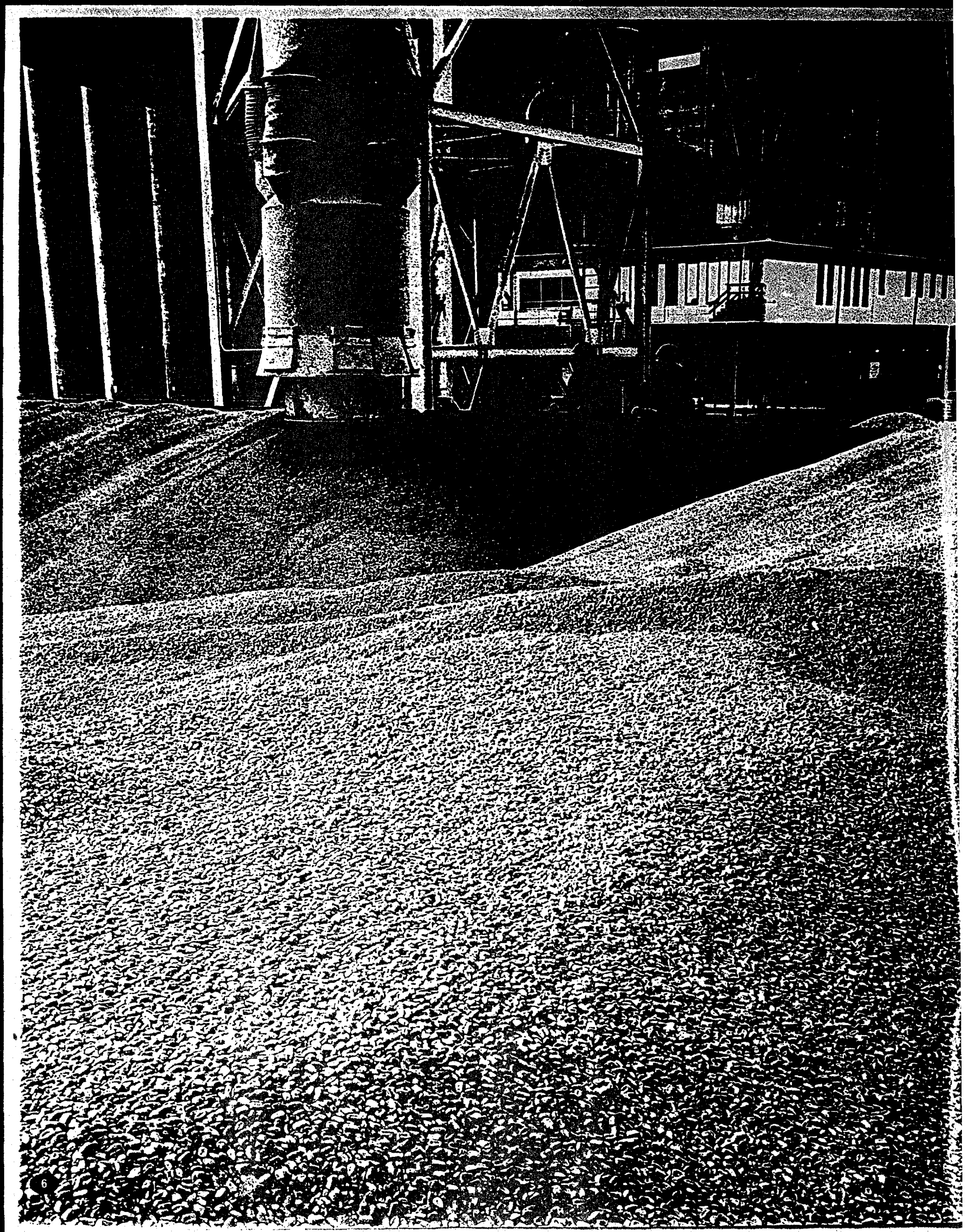
The merger of Maersk Line and Sea-Land Service, and the large new ships being introduced by the new company, resulted in a call for a 600-foot pier extension and a possible terminal expansion in Tacoma. The facility already encompasses 132 acres, and the Port owns an additional 52 vacant acres adjacent to the terminal.

The Maersk/Sea-Land merger also resulted in the creation of a new, separate, shipping entity, CSX Lines. The company operates three ships between Tacoma and Alaska. CSX also serves Hawaii and Guam from Tacoma.

Totem Ocean Trailer Express (TOTE), with service between Tacoma and Anchorage, announced that in 2002 it will launch two new ships with nearly twice the cargo capacity of its three current vessels.

Each of the Port's container shipping customers came to Tacoma looking for growth. And in every case, the Port is working with them to help ensure success. Container traffic through the Port is expected to grow by 8 percent to 1.36 million twenty-foot equivalent units (TEUs) in the year 2000, compared to 1.27 million in 1999. ■

Left: A straddle carrier makes its way through the container yard at the Evergreen Terminal.
Above: One of Maersk Sealand's massive S Class ships sits at the berth while work to extend the outreach of the container cranes at the terminal continues.



Port terminals bolster strong performance in non-containerized sectors.

Non-containerized cargo traffic through the Port began a rebound in 1999 with the stabilization of Asian economies. The Port handles a wide range of these cargoes at both leased and Port-operated facilities. Products such as grain, logs, and heavy equipment were hit hard by the devaluation of currencies throughout Asia in 1997 and 1998.

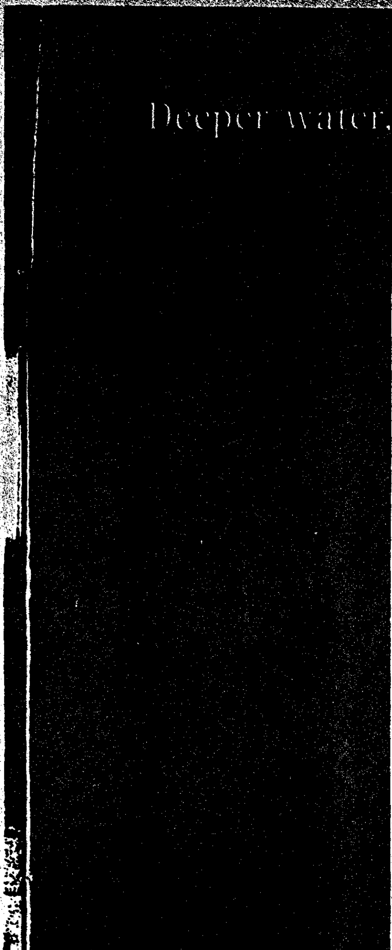
Grain exports through Tacoma grew 93 percent in 1999. Part of that growth was due to increased overseas demand. Part of it also was the result of changes similar to those taking place in the container shipping industry – companies responding to intense competition by merging with competitors. Continental Grain, the world's second-largest grain trading company and the operator of the Port's grain terminal, was purchased in 1999 by its long-time rival, Cargill, the world's largest grain trading firm.

After the purchase, Cargill consolidated most of its Puget Sound grain exports in Tacoma. The Tacoma facility has excellent rail access, deep water at the berth, and a favorable lease agreement. Those factors have allowed grain volumes to grow and have provided thousands of hours of work for local longshore labor.

Autos were another bright spot in 1999. Tacoma is already the largest auto-handling port in the state of Washington, and the 13 percent increase autos posted in 1999 solidified that position. A strong U.S. economy played an important role in generating demand for autos, and that helped create jobs and economic opportunity in Tacoma.

Major auto customers are Isuzu, Kia, Mazda, Mitsubishi and Suzuki. Auto Warehousing Company manages auto handling and processing at the Port's Pierce County Terminal. ■

Left: Grain exports through Tacoma grew 93 percent in 1999.
Above: Auto shipments saw a 13 percent increase.



Deeper water, better roads and superior rail connections ensure smooth flow of cargo.

Part of helping customers grow is ensuring that the Port's transportation network has the capacity to handle increased volumes. That means waterways have to be deep enough and wide enough to accommodate ever larger ships. Intermodal yards and other rail facilities have to be able to handle greater volumes of traffic. Roads must ensure the efficient movement of freight in and out of the Port and handle the flow of local traffic.

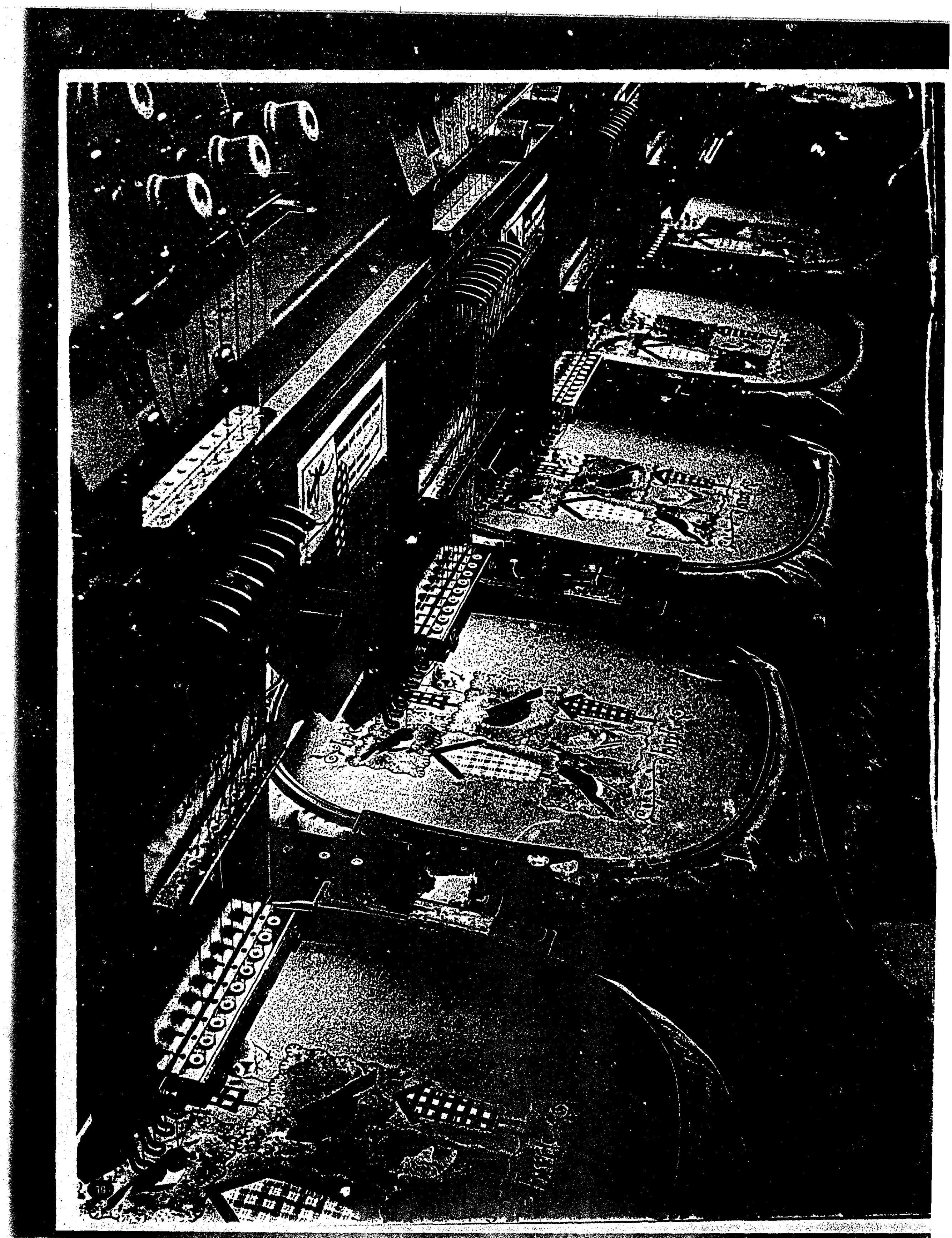
When it comes to deep water, Tacoma has a natural advantage. Commencement Bay is up to 600 feet deep, and the Port's manmade waterways do not require ongoing dredging to maintain depth. Nonetheless, the Port undertook a dredging effort in 1999 to ensure its long-term competitiveness. The 2.65-mile-long Blair Waterway is being dredged to a depth of 51 feet. The dredging project will be completed by mid-2000. The current depth ranges from 48 to 50 feet. The project will ensure that this waterway is deep enough to accommodate the draft requirements of today's largest containerships and tomorrow's vessels as well.

Ongoing rail expansions in the Port area added 10,000 feet of staging tracks in 1999 to the classification yard operated by Tacoma Rail, a unit of Tacoma Public Utilities. The Port advanced funds for the rail expansion project and will be repaid by Tacoma Rail over several years. Upgrades to the Port's North and South Intermodal yards were implemented as well, and the new Hyundai Intermodal Yard opened at Washington United Terminals in May 1999.

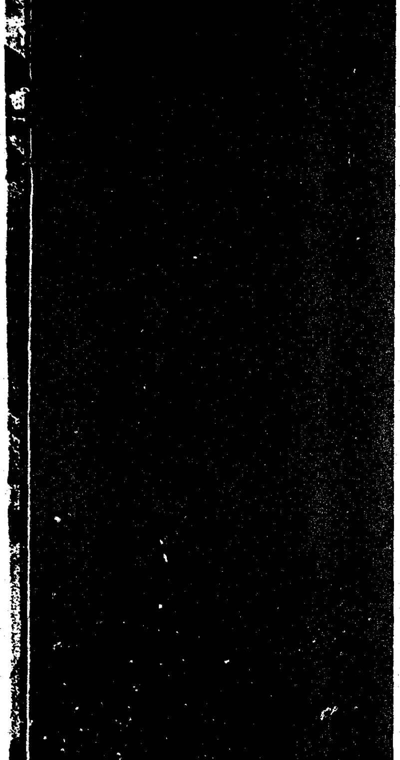
The year also saw the Port gearing up for one of the most significant road and rail expansion projects in its history, the Port of Tacoma Road Overpass project. Beginning in summer 2000, the Port and the Washington State Department of Transportation will build an overpass that will raise Port of Tacoma Road – the primary gateway to the Port – above State Route 509 and create a new interchange. The overpass also will bridge a new set of staging tracks for arriving and departing intermodal trains.

The $33 million grade-separation project will provide the road and rail capacity the Port needs to enhance growth opportunities for current customers and attract new customers. ■

Left: The Port is dredging the Blair Waterway to a depth of -51 feet to accommodate ever larger container ships.
Above: Improvements to the Port's rail infrastructure are increasing capacity and improving efficiency.

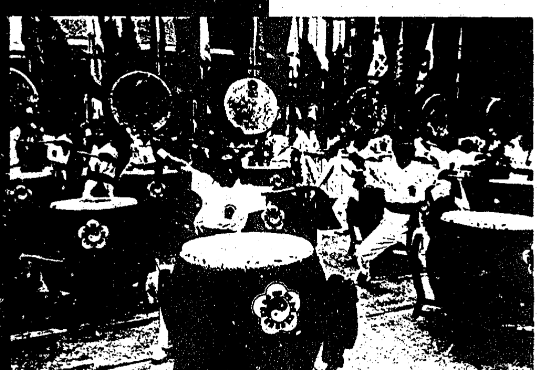


Trade promotion, cultural exchanges and support for community improvements help Tacoma thrive.



The Port has long been the focus of Tacoma's international identity. Goods from around the globe and North America have made their way to market via the Port since its creation by Pierce County voters in 1918. In an effort to capitalize on its status as a hub for international trade, and extend the benefits of trade throughout the local community, the Port embarked on a major expansion of its foreign trade zone (FTZ #86) in 1999.

The expansion will more than double the size of FTZ #86 to 1,400 acres and add 10 new properties zoned for fabrication, manufacturing and warehousing activities. Foreign trade zones give importers and exporters the flexibility to ship, store, manipulate and add value to goods while delaying or eliminating payment of U.S. Customs duties.



One of the companies that may benefit from FTZ status is Morning Sun, a designer and marketer of embroidered and screenprinted clothing. The company is located at Transpacific Industrial Park, a 1.5 million square foot development that is included in the proposed FTZ expansion.

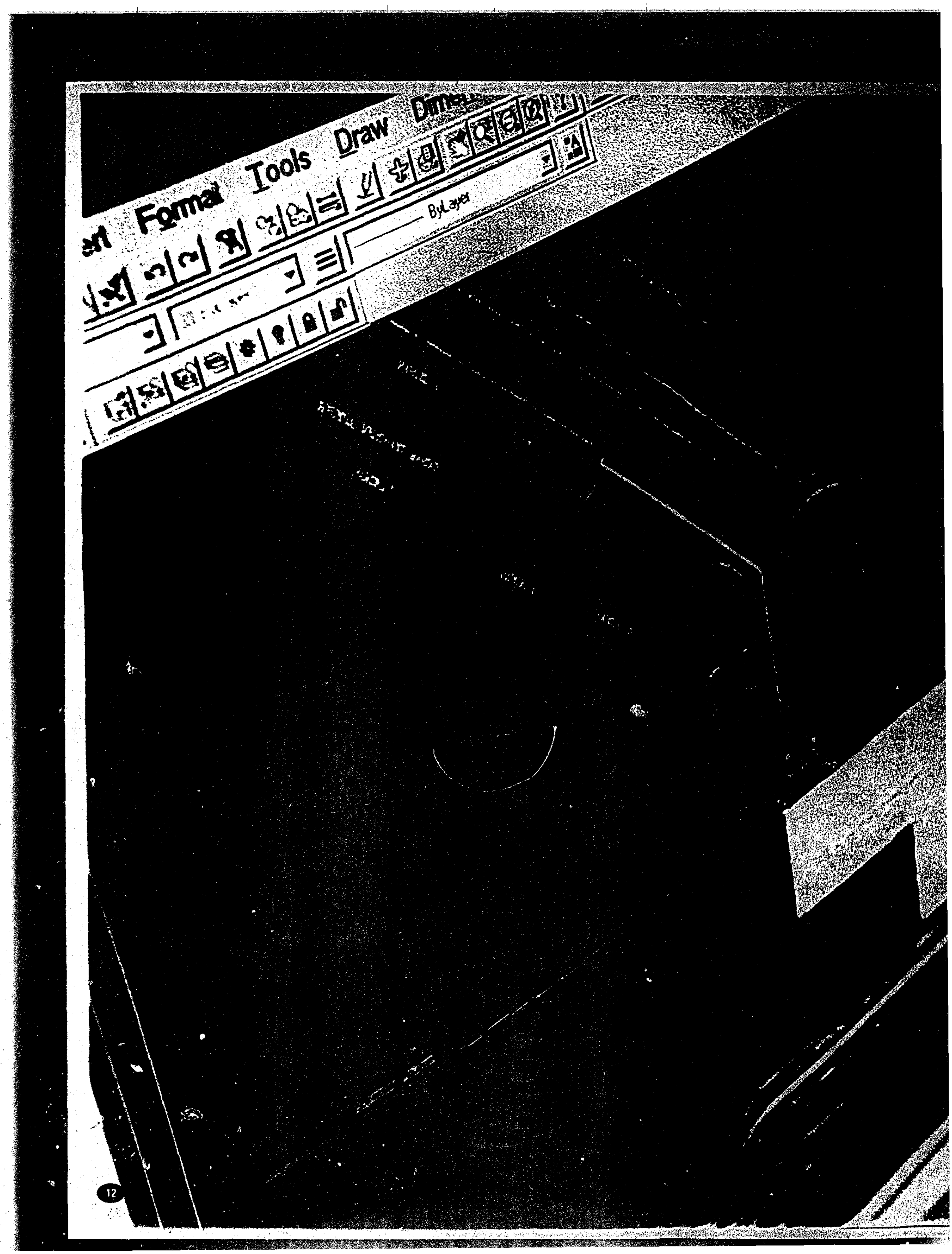
Morning Sun imports T-shirts and sweatshirts and embroiders or applies screenprints of original designs. FTZ status would help the company manage cash flow by delaying payment of import duties until value is added to the product and it is shipped to customers. That kind of competitive advantage will help draw more cargo to the Port and add jobs.

The Port also supports cultural programs that contribute to Tacoma's growing international flavor. Relationships with sister ports of Tianjin, China; Belawan, Indonesia; Kitakyushu, Japan; Vladivostok, Russia and Kaohsiung, Taiwan enliven Tacoma's cultural scene. In 1999, the Port sponsored a performance by Kaohsiung's 300-member Tai Ji Men dance group, which entertained hundreds of Tacomans.

The Port also participates in the Commencement Bay Maritime Fest, where Port employees and other teams race classic Chinese dragon boats, and thousands of visitors take Port-sponsored on-the-water tours of the harbor.

In addition, the Port supports the revitalization of Tacoma's Foss Waterway. The Port's goal is to help the east side of the waterway function as a transitional landscape, serving as a buffer between the industrial Tideflats and Tacoma's increasingly vibrant downtown. ■

Left: Shirts are embroidered at Morning Sun, a company that may benefit from the Port's foreign trade zone.
Above: The Tai Ji Men dance group from Kaohsiung, Taiwan.


Format
Tools
Draw
ByLayer

Careful planning will help ensure future success.

The Port's substantial physical advantages have been, and will continue to be, critical to its success. But using those advantages to achieve the best results demands long-range planning and diligent implementation.

In an effort to both anticipate and respond to changes in the business landscape, the Port undertook an in-depth study of its facilities and physical assets in 1999. A report based on the study, known as Vision 2020, outlines a series of options for development that will help the Port, its customers and the community enjoy the benefits of growing international trade and transportation.

The volume of containers moving through Puget Sound ports is expected to grow by 50 percent to a total of 6 million TEUs by the year 2020. Tacoma's TEU volume could nearly triple from its current level of 1.3 million to a total of 3.5 million by 2020. One of the keys to ensuring that Tacoma garners its share of growth in container trade is the availability of land for expansion.

Despite the rapid pace of container terminal development over the past 15 years, land remains one of Tacoma's most abundant resources. In fact, there are more than 1,300 acres in and around the Port with the potential for container handling activities. That's nearly 40 percent of the total potential container handling acreage in the five major U.S. West Coast container ports. Enough land to continue to provide outstanding intermodal rail yards and highway connections is also part of the Tacoma picture.

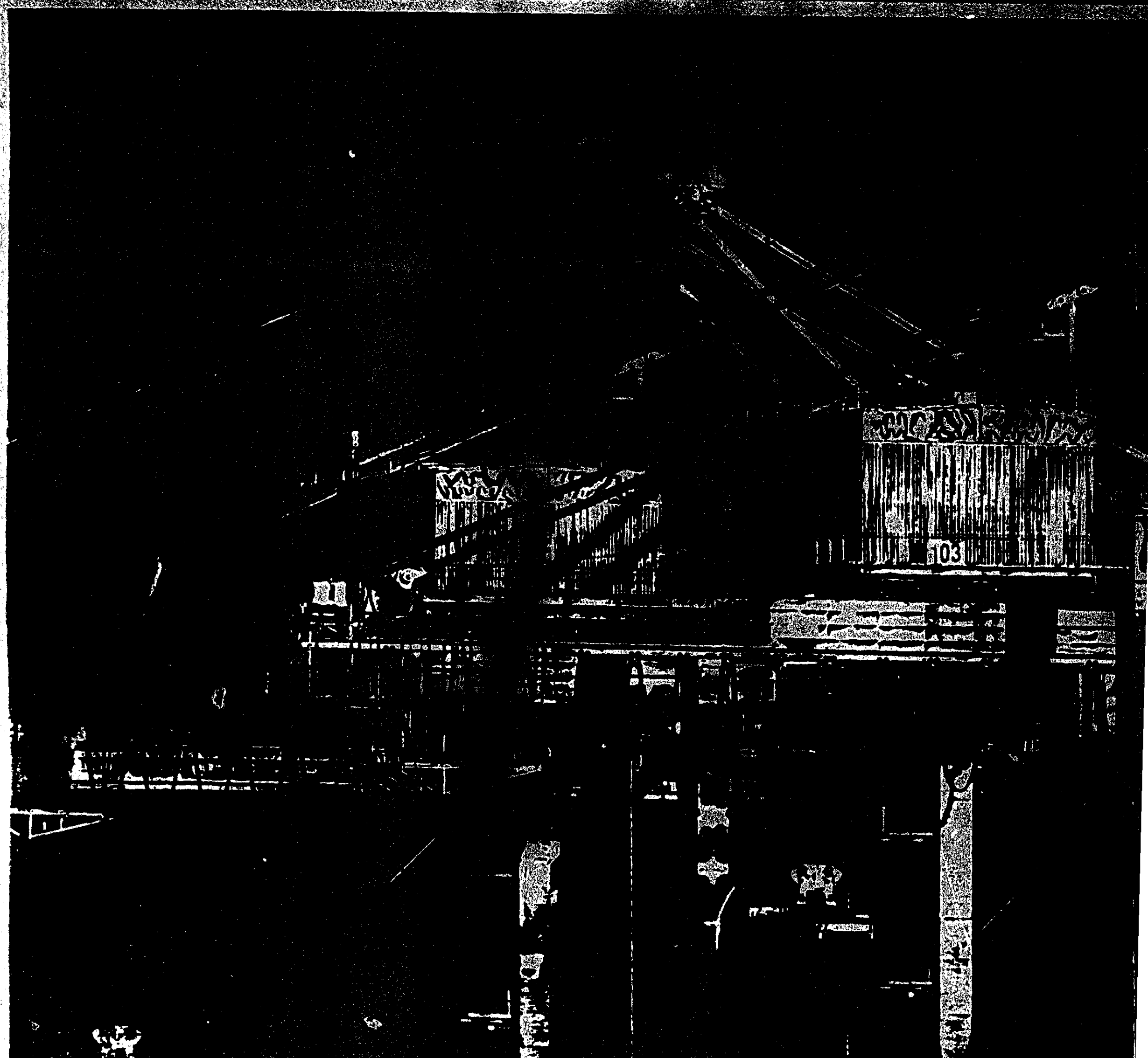
In addition, the Hylebos Waterway, which in its current configuration is not suitable for container terminal development, offers properties that might allow the Port to relocate facilities that handle autos, logs, wood chips and other non-containerized cargoes.

In 1999, the Port showed it could successfully meet the growth needs of its existing customers, as well as attract major new customers, cargoes and family-wage jobs to the Port and Pierce County.

Using Vision 2020 as a guide, the Port is confident it can continue to achieve even greater results in these areas in the years ahead. ■

Left: Computer-generated images help the Port map its future.

Above: A worker cuts steel rebar from chunks of concrete as demolition precedes construction of a new gate complex at the Evergreen Terminal.



Top 5 Trading Partners – 1999

	Value of two-way trade
Japan	$7.26 billion
Alaska	$3.48 billion
China	$3.32 billion
Taiwan	$2.00 billion
Korea	$1.64 billion

Total value of two-way trade, $20.48 billion

Source: U.S. Census Bureau (Alaska data, Port of Tacoma estimate)

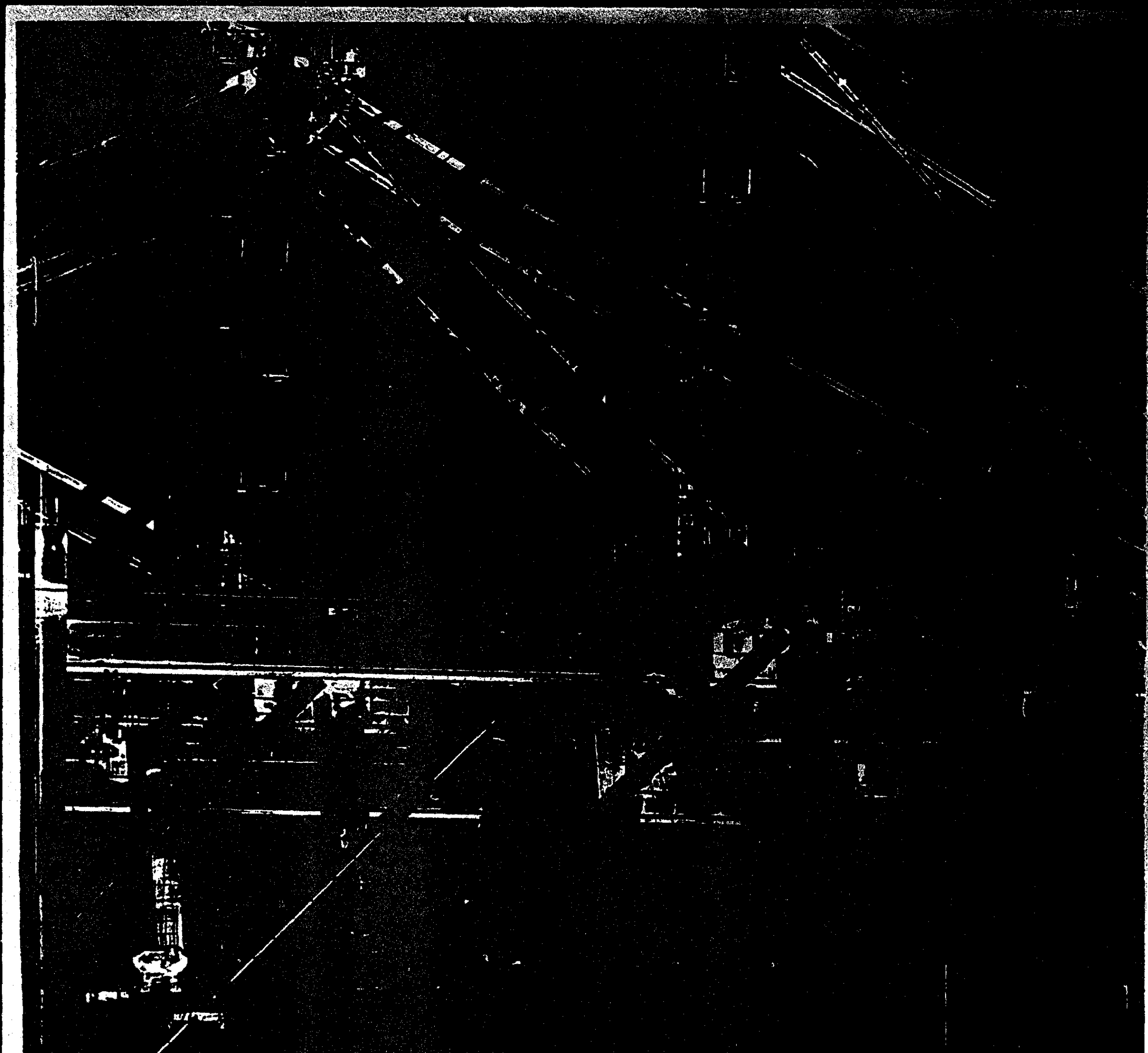
Top 5 Import Commodities – 1999

	Value
Electrical Equipment and Components	$2.52 billion
Machinery	$2.32 billion
Motor Vehicles	$2.28 billion
Toys and Sports Equipment	$0.84 billion
Footwear	$0.72 billion

Total value of imports, $13.2 billion (excludes domestic cargo)

Source: U.S. Census Bureau

Late afternoon sunshine [illegible] a golden glow on container cranes at Washington United Terminals



Top 5 Export Commodities – 1999

	Value
Machinery	$0.43 billion
Meat	$0.37 billion
Grain	$0.35 billion
Plastics	$0.27 billion
Auto Parts	$0.27 billion

Total value of exports, $3.8 billion (excludes domestic cargo)

Source: U.S. Census Bureau

Financial Highlights – 1999

	In Thousand of Dollars
Revenues	$57,238
Net Earnings	$11,546
Working Capital	$75,048
Capital Expenditures	$14,501
Land, Facilities and Equipment	$546,225
Long-term Obligations (non-current portion)	$122,412
Equity	$319,439
Debt Service Coverage Ratio	3.70

Years Ended December 31, 1999 and 1998

COMPARATIVE STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN RETAINED EARNINGS

	1999	1998
OPERATING REVENUES		
Terminal services	$ 17,015,193	$ 17,843,239
Property rentals	40,222,881	37,451,871
Environmental insurance proceeds	- -	261,921
Total operating revenues	**57,238,074**	**55,557,031**
OPERATING EXPENSES		
Operations	15,779,050	16,650,736
Maintenance	8,468,284	8,412,196
Administration	8,036,019	7,678,470
Environmental	- -	268,141
Total before depreciation	**32,283,353**	**33,009,543**
Depreciation	15,504,430	14,098,430
Total operating expenses	**47,787,783**	**47,107,973**
Operating income	**9,450,291**	**8,449,058**
NON-OPERATING REVENUES (EXPENSES)		
Ad valorem tax revenues	6,548,188	6,281,499
Interest on general obligation bonds	(2,882,256)	(2,991,607)
Net ad valorem tax revenues	**3,665,932**	**3,289,892**
Interest income	4,763,812	6,326,160
Net increase (decrease) in the fair value of investments	(2,190,656)	93,290
Interest expense	(3,949,462)	(3,095,932)
Gain on disposals of facilities and equipment	16,058	439,249
Other, net	(210,087)	(73,928)
Total non-operating revenues (expenses)	**2,095,597**	**6,978,731**
Net income	**11,545,888**	**15,427,789**
DEPRECIATION ON CONTRIBUTED ASSETS	129,884	129,884
RETAINED EARNINGS AT BEGINNING OF YEAR	301,377,092	285,819,419
Retained earnings at end of year	**$313,052,864**	**$301,377,092**

See notes to financial statements.

Comparative Balance Sheets

December 31, 1999 and 1998

ASSETS

	1999	1998
CURRENT ASSETS		
Cash and cash equivalents	$ 1,862,830	$ 1,615,673
Investments, at fair value	75,414,519	74,946,791
Trade accounts receivable, net	7,769,561	6,539,437
Taxes receivable	448,939	456,545
Prepayments and other current assets	4,725,640	4,263,684
Total current assets	**90,221,489**	**87,822,130**
PROPERTY, PLANT AND EQUIPMENT		
Land	134,258,316	129,583,297
Buildings	59,762,840	58,653,703
Improvements	264,033,266	248,555,815
Machinery and equipment	88,170,911	87,413,269
Construction in process	17,065,056	25,457,787
Total cost	**563,290,389**	**549,663,871**
Less accumulated depreciation	191,720,593	176,597,396
Net property, plant and equipment	**371,569,796**	**373,066,475**
OTHER ASSETS	**7,477,247**	**5,548,947**
Total assets	**$469,268,532**	**$466,437,552**

LIABILITIES AND FUND EQUITY

	1999	1998
CURRENT LIABILITIES		
Warrants payable	$ 283,517	$ 1,066,696
Accounts payable	3,860,283	2,195,797
Payroll and taxes payable	1,711,861	1,736,984
Retainage under construction contracts	270,594	1,452,179
Accrued interest	1,381,994	1,398,755
Current portion of long-term liabilities	7,665,000	8,715,757
Total current liabilities	**15,173,249**	**16,566,168**
LONG-TERM LIABILITIES		
General obligation bonds	50,920,000	53,755,000
Revenue bonds	70,970,000	75,800,000
Other obligations	794,242	794,242
Total long-term liabilities	**122,684,242**	**130,349,242**
Less bond discount	272,308	320,177
Net long-term liabilities	**122,411,934**	**130,029,065**
DEFERRED LIABILITIES	**12,244,466**	**11,949,324**
Total liabilities	**149,829,649**	**158,544,557**
FUND EQUITY		
Contributed capital from grants	6,386,019	6,515,903
Retained earnings, unreserved	313,052,864	301,377,092
Total fund equity	**319,438,883**	**307,892,995**
COMMITMENTS AND CONTINGENCIES	--	--
Total liabilities and fund equity	**$469,268,532**	**$466,437,552**

See notes to financial statements.

Comparative Statements of Cash Flows

Years Ended December 31, 1999 and 1998

	1999	1998
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	$ 55,947,350	$ 54,871,729
Cash paid to suppliers for goods and services	(15,108,220)	(17,017,905)
Cash paid to Longshore labor and employees	(16,572,260)	(16,708,405)
Proceeds from lawsuit settlements	- -	261,921
Net cash provided by operating activities	**24,266,870**	**21,407,340**
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Cash received for operating reserves	91,654	141,407
Cash paid for operating reserves	- -	(363,793)
Net cash provided by (used in) non-capital financing activities	**91,654**	**(222,386)**
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of property, plant and equipment	16,199	684,065
Proceeds from lawsuit settlements	- -	732,512
Principal payments on general obligation and revenue bonds, and other debts	(8,715,757)	(9,117,415)
Acquisition and construction of capital assets	(14,501,372)	(71,178,387)
Interest paid on general obligation and revenue bonds, and other debts	(7,536,584)	(8,760,166)
Cash received from property taxes for general obligation bonds	6,555,794	6,276,472
Cash received for other assets	503,930	365,818
Cash paid for other assets	(2,644,859)	(432,396)
Net cash used in capital and related financing activities	**(26,322,649)**	**(81,429,497)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(170,387,012)	(376,539,854)
Proceeds from sales and maturities of investment securities	167,793,290	429,219,105
Interest received on investments	4,805,004	7,204,018
Net cash provided by investing activities	**2,211,282**	**59,883,269**
Net increase (decrease) in cash and cash equivalents	**247,157**	**(361,274)**
CASH AND CASH EQUIVALENTS		
Beginning of year	1,615,673	1,976,947
End of year	**$ 1,862,830**	**$ 1,615,673**

	1999	1998
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income	$ 9,450,291	$ 8,449,058
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	15,504,430	14,098,430
Increase in post-retirement health care benefits	277,282	281,011
Decrease in rent prepayments	- -	(77,056)
Increase in vacation, sick and retirement benefits	40,716	146,707
Decrease in deferred income	(215,116)	(60,600)
Changes in assets and liabilities:		
Increase in accounts receivable	(1,230,124)	(285,725)
Increase in prepayments	(429,234)	(326,711)
Decrease in other assets	12,441	62,775
Increase (decrease) in warrants payable	(783,179)	759,737
Increase (decrease) in accounts payable	1,664,486	(2,083,070)
Increase (decrease) in payroll and taxes payable	(25,123)	442,784
Total adjustments and changes	**14,816,579**	**12,958,282**
Net cash provided by operating activities	**$24,266,870**	**$21,407,340**
SUPPLEMENTAL DISCLOSURES OF NON-CASH CAPITAL AND FINANCING ACTIVITIES		
Receivable from lawsuit settlement	$ - -	$ 248,000
Financed additions to property, plant and equipment	- -	258,650

See notes to financial statements.

December 31, 1999 and 1998

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Port of Tacoma (the Port) have been prepared in conformity with generally accepted accounting principles as applied to government units. The Governmental Accounting Standards Board is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the Port's accounting policies are described below:

REPORTING ENTITY

The Port is a municipal corporation of the State of Washington created in 1918 under provisions of the Revised Code of Washington 53.04.010 et seq. The Port has geographic boundaries coextensive with Pierce County, Washington, and is situated on Commencement Bay in Puget Sound.

The Port is independent from Pierce County government and is administered by a five-member Board of Commissioners elected by Pierce County voters. The Commission delegates administrative authority to an Executive Director and administrative staff to conduct operations of the Port. The County levies and collects taxes on behalf of the Port. Pierce County provides no funding to the Port. Additionally, Pierce County does not hold title to any of the Port's assets, nor does it have any right to the Port's surpluses.

NATURE OF BUSINESS

The Port is authorized by Washington law to provide and charge rentals, tariffs and other fees for docks, wharves and similar harbor facilities, including associated storage and traffic handling facilities, for waterborne commerce. The Port may also provide freight and passenger terminals and transfer and storage facilities for other modes of transportation, including air, rail and motor vehicles. The Port may acquire and improve lands for sale or lease for industrial or commercial purposes, and may create industrial development districts.

BASIS OF ACCOUNTING AND PRESENTATION

The accounting policies of the Port conform to generally accepted accounting principles, as applicable to proprietary funds of governmental units. The Port has chosen to use Financial Accounting Standards Board pronouncements issued after November 30, 1989 when there are no applicable Government Accounting Standards Board Statements.

The accounting records of the Port are maintained in accordance with methods prescribed by the State Auditor under the authority of Chapter 43.09, Revised Code of Washington. The Port also follows the Uniform System of Accounts for Port Districts in the State of Washington.

The Port uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Property, plant and equipment purchases are capitalized, and long-term liabilities are accounted for in the appropriate funds.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

ASSETS, DEPRECIATION AND AMORTIZATION

Capital assets are recorded at cost. Donations by developers are recorded at fair market value on the date donated.

Interest on funds used during construction, less interest earned on related interest-bearing investments if the asset is financed with the proceeds from externally restricted tax-exempt proceeds, is capitalized as part of the cost of the asset. This process is intended to remove the cost of financing construction activity from the comparative statements of revenues, expenses and changes in retained earnings, and to treat such cost in the same manner as construction labor and material costs.

Depreciation is computed on the straight-line method. The following lives are used:

Buildings and improvements	20 - 50 years
Machinery and equipment	5 - 25 years

Preliminary costs incurred for proposed projects are deferred pending construction of the facility. Costs relating to projects ultimately constructed are transferred to the appropriate capital asset account; charges that relate to abandoned projects are expensed when the project is abandoned.

ENVIRONMENTAL REMEDIATION COSTS

The Port accrues for losses associated with environmental remediation obligations when such losses are probable and reasonably estimable. Accruals for estimated losses from environmental remediation obligations generally are recognized no later than completion of the remedial feasibility study. Such accruals are adjusted as further information develops or circumstances change. Costs of future expenditures for environmental remediation obligations are discounted to their present value. Recoveries of environmental remediation costs from other parties are recorded as assets when their receipt is deemed probable. At December 31, 1999 and 1998, the estimated environmental remediation liability was $2,888,000, net of a $344,000 (6%) discount

INVENTORIES

Inventories, which are included in prepayments and other current assets, are valued at net realizable value, which approximates cost, using the first-in, first-out method.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents, represent cash, demand deposits and overnight investments.

INVESTMENTS

Investments are stated at fair value. Interest on debt securities is recognized in non-operating revenues as earned. Changes in the fair value of investments are also included in non-operating revenues (expenses).

AMORTIZATION OF CONTRIBUTED CAPITAL

Depreciation and amortization expense totaled $129,884 annually for 1999 and 1998, applicable to assets acquired from grants. In accordance with the Port's accounting policy for grant assets, equity from grants is reduced by such depreciation.

VACATION AND SICK LEAVE BENEFITS

The Port accrues unpaid vacation and sick leave benefit amounts as earned and payable upon termination. Accrued vacation and sick leave, included in operating reserves, amount to $968,229 and $1,481,273, respectively, at December 31, 1999, and $918,236 and $1,512,525, respectively, at December 31, 1998.

UNAMORTIZED DEBT EXPENSE

Costs relating to the sale of bonds are included in other assets. The costs are deferred and amortized over the lives of the various bond issues.

CAPITALIZED INTEREST

The Port follows the policy of capitalizing interest as a component of the cost of property, plant and equipment constructed for its own use. During 1999 total interest incurred was $4,637,567, of which $3,949,462 was charged to operations and $688,105 was capitalized. During 1998 total interest incurred was $5,031,429, of which $3,095,932 was charged to operations and $1,935,497 was capitalized.

RECENT ACCOUNTING PRONOUNCEMENTS

In June 1999, the Government Accounting Standards Board issued GASB No. 34, *Basic Financial Statements and Management Discussion and Analysis for State and Local Governments*. This statement requires special purpose governments to redraft their financial statements to include a section for management discussion and analysis, enterprise fund financial statements (defined to include a statement of net assets, a statement of revenues, expenses and changes in fund net assets; and a statement of cash flows), notes to the financial statements and required supplementary information. This statement is effective for the Port for fiscal years beginning after June 30, 2003. The Port does not anticipate that the adoption of GASB No. 34 will have a material effect on its financial position or results of operations.

RECLASSIFICATION

Certain items in the 1998 financial statements have been reclassified to conform with classifications adopted for 1999. There was no effect on net income previously reported.

NOTE 2 - DEPOSITS AND INVESTMENTS OF DISCRETIONARY FUNDS

DISCRETIONARY DEPOSITS

The carrying amount of the Port's demand deposits as of December 31, 1999 was $1,862,830. Of the bank balances, $200,000 was covered by federal depository insurance. The remaining balance of $1,662,830 was uninsured and uncollateralized. Of the Port's certificates of deposit and accrued interest shown below, $200,000 was covered by federal depository insurance, and the remaining $1,511,746 (1998 - $638,348) was fully collateralized and protected under the Washington Public Protection Act. These certificates of deposit were registered, and held by its agent in the Port's name.

NOTE 2 - DEPOSITS AND INVESTMENTS OF DISCRETIONARY FUNDS *continued*

	1999 Cost	1999 Fair Value	1998 Cost	1998 Fair Value
Certificates of deposit	**$1,711,746**	**$1,711,746**	**$838,348**	**$838,348**

DISCRETIONARY INVESTMENTS

The Port used quoted market price to estimate the fair value of all investments. Realized gains and losses on investments that have been held more than one fiscal year and sold in the current year are included as a change in the fair value of investments.

The Port's investments are categorized to give an indication of the risk assumed at year-end. Category 1 includes investments that are either insured, registered or held by the Port or its agent in the Port's name. Category 2 includes uninsured and unregistered investments which are held by the counterparty's trust department or agent in the Port's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty or its trust department or agent but not in the Port's name. The Port does not have any Category 2 or 3 investments at December 31, 1999 and 1998.

All of the Port's discretionary investments as of December 31, 1999 and 1998 are Category 1 investments and are summarized below:

	1999 Amortized Cost	1999 Fair Value	1998 Amortized Cost	1998 Fair Value
Bankers' acceptances	$12,042,904	$12,268,168	$12,671,365	$12,798,176
Government securities	63,626,206	61,434,605	60,700,676	60,798,026
Federal agency securities	--	--	512,083	512,241
	75,669,110	**73,702,773**	**73,884,124**	**74,108,443**
Total discretionary investments	**$77,380,856**	**$75,414,519**	**$74,722,472**	**$74,946,791**

The amortized cost and fair value of all discretionary securities classified by contractual maturity as of December 31, 1999 and 1998 are as follows:

	1999 Amortized Cost	1999 Fair Value	1998 Amortized Cost	1998 Fair Value
Due within one year	$38,059,275	$38,435,909	$45,089,339	$45,368,038
Due after one year through three years	3,291,652	3,269,322	4,260,664	4,302,763
Due after three years through five years	7,128,171	6,954,940	4,589,691	4,596,949
Due after five years	28,901,758	26,754,348	20,782,778	20,679,041
	$77,380,856	**$75,414,519**	**$74,722,472**	**$74,946,791**

State of Washington statutes authorize the Port to invest in direct obligations of the U.S. Government, certificates of deposit, bankers' acceptances, and repurchase agreements. These investments must be placed with or through qualified public depositories of the State of Washington. The investments in U.S. Treasury Bills and U.S. Treasury Notes (included in Government securities), federal agency securities, bankers' acceptances, and certificates of deposit are protected under the Washington Public Protection Act. The effective interest rates ranged from 4.6% to 9.0% at December 31, 1999 and 1998.

NOTE 3 - PROPERTY, PLANT AND EQUIPMENT

The following activity took place in property, plant and equipment during the current year:

	Cost at January 1, 1999	Additions and Transfers	Deletions and Transfers	Cost at December 31, 1999
Land	$129,583,297	$ 4,675,019	$ --	$134,258,316
Buildings	58,653,703	1,109,137	--	59,762,840
Improvements	248,555,815	15,477,451	--	264,033,266
Machinery and equipment	87,413,269	1,139,812	382,170	88,170,911
Construction in process	25,457,787	16,660,216	25,052,947	17,065,056
Total property, plant and equipment	**$549,663,871**	**$39,061,635**	**$25,435,117**	**$563,290,389**

NOTE 4 - LONG-TERM LIABILITIES

Long-term liabilities at December 31 consist of the following:

Description and Date of Issue		Original Interest Rate	Earliest Year of Call	Last Year of Maturity	1999	1998
GENERAL OBLIGATION BONDS						
05/15/91	A	6.00 - 9.00%	2001	2011	$ 1,530,000	$ 2,225,000
07/15/92		2.90 - 5.60%	*	2004	1,675,000	1,970,000
12/15/94		4.90 - 6.25%	*	2009	7,910,000	8,475,000
10/01/97	A	4.30 - 5.00%	*	2009	10,655,000	10,655,000
10/01/97	B	3.80 - 5.50%	2007	2017	31,985,000	32,290,000
					53,755,000	**55,615,000**
Less current portion					2,835,000	1,860,000
Total long-term general obligation bonds, net of current portion					**$50,920,000**	**$53,755,000**
REVENUE BONDS						
10/01/91		5.3 - 6.9%	2001	2008	$20,900,000	$21,250,000
07/15/92		2.5 - 5.6%	2002	2005	20,300,000	23,380,000
10/01/97		4.6 - 5.5%	2007	2017	34,600,000	34,600,000
					75,800,000	**79,230,000**
Less current portion					4,830,000	3,430,000
Total long-term revenue bonds, net of current portion					**$70,970,000**	**$75,800,000**
OTHER LONG-TERM OBLIGATIONS						
Natural resource damages		6.90%	*	1999	$ --	$3,425,757
Real estate contracts		5.20 - 8.00%	*	2016	794,242	794,242
					794,242	**4,219,999**
Less current portion					--	3,425,757
Total other long-term obligations, net of current portion					**$ 794,242**	**$ 794,242**
Total current portion of long-term liabilities					**$7,665,000**	**$8,715,757**

*Currently callable

The general obligation bonds and related interest are paid from ad valorem tax revenues. The revenue bonds are secured by a pledge of the Port's gross revenues.

During 1997 the Port issued three separate bond issues, and a portion of the funds received was used to refund certain debt obligations. These funds were placed in an irrevocable trust providing for all future debt service payments on the defeased debt. The liability for this defeased debt was appropriately removed from the Port's balance sheets. The balance of the defeased bonds at December 31, 1999 totaled $17,660,000.

Annual Debt Amortization

The annual requirements to amortize all debt outstanding as of December 31, 1999, including interest, are as follows:

	General Obligation	Other Obligations	Revenue	Totals
2000	$ 5,608,926	$ 50,000	$ 9,117,065	$ 14,775,991
2001	5,595,539	50,000	9,122,280	14,767,819
2002	5,599,849	100,000	9,120,520	14,820,369
2003	5,591,681	100,000	9,120,680	14,812,361
2004	5,593,461	100,000	9,122,050	14,815,511
2005	5,663,921	100,000	9,126,205	14,890,126
2006	5,664,588	100,000	9,264,053	15,028,641
2007	5,667,809	150,000	9,260,562	15,078,371
2008	5,667,469	150,000	9,230,925	15,048,394
2009	5,667,406	150,000	3,008,500	8,825,906
2010	4,460,281	150,000	3,008,250	7,618,531
2011	4,486,956	150,000	3,006,250	7,643,206
2012	2,111,200	200,000	3,003,625	5,314,825
2013	2,113,200	200,000	3,003,965	5,317,165
2014	2,112,920	200,000	3,006,005	5,318,925
2015	2,113,220	200,000	3,006,420	5,319,640
2016	2,113,840	200,000	3,004,945	5,318,785
2017	2,114,520	200,000	3,006,315	5,120,835
Total	**$77,946,786**	**$2,550,000**	**$109,538,615**	**$190,035,401**

Future maturities of long-term obligations are as follows:

Year	
2000	$ 7,665,000
2001	8,060,000
2002	8,460,000
2003	8,885,000
2004 - 2017	97,279,242
	$130,349,242

General Obligation Bonds

Revised Code of Washington (RCW) Chapter 53.36 provides that nonvoted general obligation bond debt cannot be incurred in excess of 0.25% of the assessed value of the taxable property in the Port district, which was $37,932,381,976 at December 31, 1999. The Port is in compliance with this limitation.

RCW Chapter 53.36 also provides that additional general obligation bond debt can be incurred upon approval by the voters of the Port district.

The paying agent for bonded debt is:

The Bank of New York
Fiscal Agencies - 7 East
101 Barclay Street
New York, NY 10286

NOTE 5 - RISK MANAGEMENT

The Port is exposed to various risks of loss related to torts; damage to, theft of and destruction of assets or cargo; natural disasters; and employee injuries. To limit its exposure, the Port purchases a variety of insurance policies, with limits to $50 million for general liability, and blanket limits for property with sub-limits of $150 million for earthquake and flood coverage. With the exception of losses which may arise from employee injuries or earthquakes, no deductible exceeds $100,000. The deductible for excess workers' compensation coverage is $275,000. Insurance coverage for earthquake damage is subject to a deductible defined as 2% of the value of the damaged property, with a minimum of $100,000. Insurance coverage for the past three years has been sufficient to cover all claim settlements.

During 1999, the Port became self-insured for its regular medical coverage. Included in operating reserves in the accompanying financial statements is the liability for unpaid claims totaling $513,633. There were no material amounts of incurred but not reported claims as of year end. Excess loss coverage has been purchased through an outside provider to limit individual loss to $50,000. Total expense charged to this new plan during 1999 was approximately $538,000.

The Port began a self-insurance program for workers' compensation in 1986. At December 31, 1999, the estimated insurance liability was $110,882 for workers' compensation. The Port carries excess workers' compensation insurance that covers losses greater than $275,000 for each accident. The liability for unpaid claims represents the estimated future medical costs and lost wages that would normally be incurred for injuries already sustained but not completely settled.

	1999	1998
Claims liability, beginning of year	$ 85,016	$112,430
Claims incurred during the year	173,957	103,974
Changes in estimate for prior year claims	127,409	73,554
Payments on claims	(275,500)	(204,942)
Claims liability, end of year	**$110,882**	**$ 85,016**

There was no liability for unemployment. At December 31, 1999 and 1998, cash reserves for workers' compensation were $325,000 and $343,457, respectively.

NOTE 6 - LEASE COMMITMENTS

The Port leases land, office space and other equipment under operating leases. Minimum future lease payments under noncancellable operating leases are as follows:

Year	
2000	$ 598,327
2001	598,327
2002	602,077
2003	602,077
2004 and thereafter	7,245,501
Total minimum payments required	**$9,646,309**

The lease term of the primary operating lease is from January 1988 to April 2015, with four successive five-year renewal options. Presently, the Port is subleasing the space for $30,937 per month for the lease term through April 2015, with two successive five-year options. Total rent expense for the years ended December 31, 1999 and 1998 was $731,804 and $795,385, respectively.

The Port, as a lessor, leases land and facilities under terms of one to fifty years. In addition, some properties are rented on a month-to-month basis. Minimum future rentals receivable under noncancellable operating leases and subleases are as follows:

Year	
2000	$ 24,354,894
2001	19,391,611
2002	20,299,030
2003	19,058,540
2004 and thereafter	265,518,035
Total minimum future rentals receivable	**$348,622,110**

Assets held for rental and leasing purposes as of December 31 are as follows:

	1999	1998
Land	$ 48,522,381	$ 46,519,492
Structures, improvements and equipment - net	207,284,653	169,587,518
Total	**$255,807,035**	**$216,107,010**

NOTE 7 - PENSION PLANS

Substantially all of the Port's full-time and qualifying part-time employees participate in one of the following statewide local government retirement systems administered by the Department of Retirement Systems, under cost-sharing multiple-employer defined benefit public employee retirement systems.

Historical trend and other information regarding each plan is presented in the State Department of Retirement Systems 1998 annual financial report. A copy of this report may be obtained at:

Department of Retirement Systems
Capital Plaza Building
1025 E. Union Street
P. O. Box 48380
Olympia, WA 98504-8380

NOTE 7 - PENSION PLANS *continued*

Public Employees' Retirement System (PERS) Plan 1 and 2

The State Legislature established PERS in 1947 under Chapter 41.40 RCW. PERS is a cost-sharing multiple-employer defined benefit system. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals and Superior courts (other than Judges); employees of legislative committees; college and university employees not in national higher education retirement programs; judges of district and municipal courts; non-certificated employees of school districts; and employees of local governments. Approximately 51% of PERS 1 salaries and 44% of PERS 2 salaries are paid to state employees.

PERS contains two plans. As used in this context, the term *plans* refers to tiers within PERS. The actual plan is PERS. Participants who joined the system by September 30, 1977 are Plan 1 members. Those joining thereafter are enrolled in Plan 2. Retirement benefits are financed from employee and employer contributions and investment earnings. Retirement benefits in both Plan 1 and Plan 2 are vested after completion of five years of eligible service.

Plan 1 members are eligible for retirement after 30 years of service, at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2% of the final average salary per year of service, capped at 60%.

Plan 2 members may retire at the age of 65 with five years of service, or at 55 with 20 years of service, with an allowance of 2% per year of service of the final average salary. Plan 2 retirements prior to 65 are actuarially reduced. There is no cap on years of service credit and a cost-of-living allowance is granted, capped at 3% annually.

During the 1997 Washington State Legislative Session, the Washington State Legislature approved a change in retirement law that became effective in 1998. Chapter 122, Laws of 1997, authorizes portability for LEOFF 1. As a result of this change, the State's contribution rate increased .01%. The material changes made during the 1997 Legislative Session that became effective during the 1998 fiscal year were disclosed in last year's annual report. None of the other bills that passed affected contribution rates.

Each biennium the Legislature establishes Plan 1 employer contribution rates and Plan 2 employer and employee contribution rates. Employee contribution rates for Plan 1 are established by legislative statute and do not vary from year to year. Employer rates from Plan 1 are not necessarily adequate to fully fund the system. The employer and employee contribution rates for Plan 2 are developed by the Office of State Actuary to fully fund the system. All employers are required to contribute at the level established by the Legislature. The methods used to determine the contribution requirements were established under state statute.

The required contribution rates, expressed as a percentage of covered payroll, as of December 31, 1999 were:

	PERS Plan 1	PERS Plan 2
Employer	4.41%	4.41%
Employee	6.00%	1.85%

Both the Port and the employees made the required contributions. The Port's required contributions for the years ended December 31 were:

	PERS Plan 1	PERS Plan 2
1999	$337,237	$ 869,668
1998	398,545	1,076,163

NOTE 8 - POST-RETIREMENT HEALTH CARE BENEFITS

In addition to providing pension benefits, the Port provides certain health care benefits for retired employees. These benefits are provided through insurance companies whose premiums are based on claims paid during the year. This became effective in August 1975 for retirees ages 60 to 65. In December 1982, benefits were extended to age 70. The plan provides major medical coverage, subject to a deductible, and a maximum benefit limit of $1,000,000 per person.

Retirees from the Port with a minimum of 15 years of service are eligible for post-retirement medical benefits upon attainment of age 60. In order to participate, qualifying retirees who retire prior to age 60 must reimburse the Port for premiums until attainment of age 60. As of December 31, 1999, 30 employees are receiving benefits.

The total unfunded liability as of December 31, 1999 of $4,426,100 (1998 - $4,148,818) has been recognized for post-retirement health care benefits and is included in operating reserves on the comparative balance sheets. The accrued liability represents the actuarial present value of accumulated benefits. The increase in the accrued liability was recognized as follows:

	1999	1998
Service cost	$195,107	$175,678
Net loss	144,691	205,868
Payments made	(62,516)	(100,535)
Net increase in liability	**$277,282**	**$281,011**

The service cost represents 1.5% of current year compensation of active employees covered by the plan. The primary assumptions used to determine the post-retirement health care liability are:

	1999	1998
Discount	7.0%	7.0%
Health care cost increase	6.8%	7.4%

The approximate effect of a 1% increase in the assumed annual health care cost is a $550,000 increase in the accrued liability, while a 1% decrease in the assumed annual health care cost results in a $475,000 decrease in the accrued liability.

NOTE 9 - DEFERRED COMPENSATION PLAN

The Port offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all Port employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

NOTE 10 - PROPERTY TAXES

The County Treasurer acts as an agent to collect property taxes levied in the County for all taxing authorities. Taxes are levied annually on January 1 on property values listed as of the prior May 31. The lien date is January 1. Assessed values are established by the County Assessor at 100% of fair market value. A revaluation of all property is required every six years.

Taxes are due in two equal installments on April 30 and October 31. Collections are distributed monthly to the Port by the County Treasurer.

The Port is permitted by law to levy up to 45 cents per $1,000 of assessed valuation for general Port purposes. The rate may be reduced for either of the following reasons:

(a) Washington State law in Revised Code of Washington (RCW) 84.55 limits the growth of regular property taxes, but it allows additional amounts for new construction. The Port is allowed to raise revenues in excess of the limit if approved by a majority of the voters as provided in RCW 84.55.050.

(b) The Port may voluntarily levy taxes at a lower rate.

Special levies approved by the voters are not subject to the above limitations.

For 1999, the Port's regular tax levy was $0.1859 per $1,000 on a total assessed valuation of $35,244,911,558, for a total regular levy of $6,548,188. In 1998, the regular levy was $6,281,499.

NOTE 11 - PORT OPERATIONS BY INDUSTRY

The Port operates principally in two industries — terminal services and property rentals. Terminal services involve marine-oriented services and include dockage, cargo handling, storage, and related activities. Properties rented include facilities and land used primarily for container terminals, industrial activities and storage.

Revenue and income from operations for the years ended December 31, and identifiable assets by industry segment, are presented below (dollars in thousands):

	1999	1998
OPERATING REVENUES		
Terminal services	$17,015	$17,843
Property rentals	40,223	37,452
Environmental insurance proceeds	--	262
Total operating revenues	**$57,238**	**$55,557**
INCOME FROM OPERATIONS		
Terminal services	$ 2,986	$ 3,949
Property rentals	15,175	13,001
	18,161	**16,950**
Administration expenses	(8,036)	(7,678)
Depreciation expense allocated to administration	(675)	(817)
Net environmental costs	---	(6)
Income from operations	**9,450**	**8,449**
NON-OPERATING REVENUES (EXPENSES) – NET	2,096	6,979
Net income	**$11,546**	**$15,428**
IDENTIFIABLE ASSETS		
Land, facilities and equipment - net:		
Terminal services	$ 93,750	$ 88,415
Property rentals	255,807	216,107
Current assets:		
Terminal services	7,770	9,183
Property rentals	104	336
Total identifiable assets	**357,431**	**314,041**
GENERAL PORT ASSETS - NET	111,838	152,397
Total assets	**$469,269**	**$466,438**
CAPITAL EXPENDITURES		
Terminal services	$ 2,513	$ 2,536
Property rentals	11,495	64,313
Total capital expenditures	**$14,008**	**$66,849**

General Port assets are principally cash, temporary investments, construction work in process, Port offices, taxes receivable, and deferred and other assets.

NOTE 12 - COMMITMENTS

The Port has entered into contractual agreements for the acquisition of equipment and construction of facilities, as well as for certain repairs. At December 31, 1999, these commitments aggregated $6,930,000.

NOTE 13 - CONTINGENCIES

The Port owns land within the boundaries of the Commencement Bay Near Shore Tideflats Superfund Site, for which a Remedial Investigation and a Feasibility Study have been performed by the U.S. Environmental Protection Agency and the Washington State Department of Ecology, pursuant to the Federal Comprehensive Environmental Response Compensation and Liability Act and the Model Toxics Control Act. Remedial actions are currently underway or complete at all known sites.

NOTE 14 - MAJOR CUSTOMER

Net revenues for the year ended December 31, 1999 and 1998 included $8,673,000 and $27,820,000, respectively, from one corporation. Receivables from that corporation totaled $2,099,000 and $3,164,000 at December 31, 1999 and 1998.

NOTE 15 - CONTRIBUTED CAPITAL

The following changes occurred in contributed capital during the years ended December 31:

	1999	1998
Contributed capital, beginning of year	$6,515,903	$6,645,787
Depreciation on contributed assets	(129,884)	(129,884)
Contributed capital, end of year	**$6,386,019**	**$6,515,903**

KNIGHT VALE
& GREGORY PLLC
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

February 10, 2000

The Board of Commissioners
PORT OF TACOMA
Tacoma, Washington

We have audited the accompanying comparative balance sheets of **PORT OF TACOMA** as of December 31, 1999 and 1998, and the related comparative statements of revenues, expenses and changes in retained earnings, and of cash flows for the years then ended. These comparative statements are the responsibility of **PORT OF TACOMA'S** management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

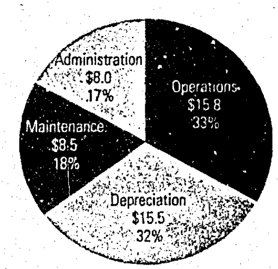
In our opinion the financial statements referred to above present fairly, in all material respects, the financial position of **PORT OF TACOMA** as of December 31, 1999 and 1998, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles.

Knight Vale & Gregory PLLC

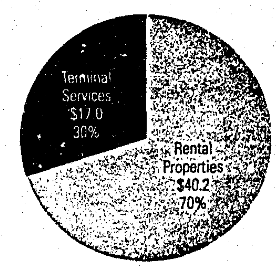
1145 Broadway Plaza, Suite 900 Tacoma, WA 98402-3523
p: 253.572.7111 f: 253-272-3143 www.kvg.com

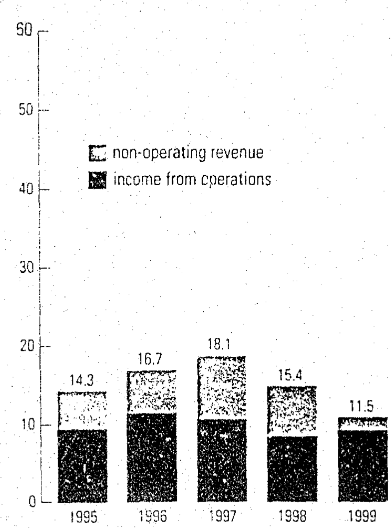
Financial Summary

1999 Operating Expenses
$47.8 million

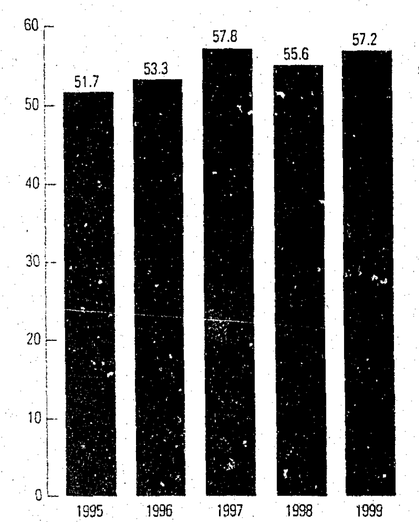


1999 Revenues
$57.2 million





Net Income
(Millions of Dollars)



Gross Operating Revenue
(Millions of Dollars)

Information for Bondholders

This information is provided as a convenience to bondholders and other institutions to assist them in reviewing historic financial information.

Comparative Schedule of Net Revenues Available for Debt Service

	1999	1998	1997	1996 (restated)	1995
REVENUES					
Terminal services	$17,015,913	$ 17,843,239	$21,292,585	$20,135,606	$20,318,716
Property rentals	40,222,881	37,451,871	35,722,089	33,130,116	31,418,696
Environmental insurance proceeds	--	261,921	774,271	5,066,869	--
Total operating revenues	**57,238,074**	**55,557,031**	**57,788,945**	**58,332,591**	**51,737,412**
Non-operating revenues (1) and (2)	2,522,135	6,429,561	4,603,634	4,320,694	4,639,092
Total revenues available for debt service	**59,760,209**	**61,986,592**	**62,392,579**	**62,653,285**	**56,376,504**
EXPENSES					
Operations	15,779,050	16,650,736	18,597,679	17,624,974	17,178,541
Maintenance	8,468,284	8,412,196	7,726,862	6,805,071	7,518,002
Administration	8,036,019	7,678,470	7,177,262	6,765,266	6,432,957
Environmental	--	268,141	30,954	890,701	--
Total operating expenses, excluding depreciation	**32,283,353**	**33,009,543**	**33,532,757**	**32,086,012**	**31,120,500**
Non-operating expenses (3)	26,799	29,396	106,365	58,895	414,123
	32,310,152	**33,038,939**	**33,639,122**	**32,144,907**	**31,534,623**
Less levy available for capital improvement (4)	1,789,136	1,295,874	--	--	--
Net expenses	**30,521,016**	**31,743,065**	**33,639,122**	**32,144,907**	**31,534,623**
Net revenues available for debt service	**$29,239,193**	**$ 30,243,527**	**$28,753,457**	**$30,508,378**	**$24,841,881**
Debt service	$ 7,892,765	$ 8,185,132	$ 6,105,816	$ 6,100,147	$ 6,100,503
DEBT SERVICE COVERAGE	**3.70**	**3.69**	**4.71**	**5.00**	**4.07**

NOTE: Above schedule does not include levies for general obligation bond issues outstanding.

FOOTNOTES:

	1999	1998	1997	1996 (restated)	1995
(1) Included in non-operating revenues is interest earned on investments of:					
1991 Revenue Bond Redemption Fund	$ 1,311	$ 25,622	$ 34,145	$ 23,874	$ 34,489
1992 Revenue Bond Redemption Fund	125,500	96,682	78,647	32,770	122,292
1997 Revenue Bond Redemption Fund	18,742	25,049	--	--	--
(2) Excluded from non-operating revenues is gain (loss) on sale or write down of property	16,058	439,249	2,052,014	289,034	(102,798)
(3) Excluded from non-operating expenses are cost of bond issue	143,828	143,828	105,497	92,242	91,604

(4) Washington Port Districts are authorized by statute to levy $0.45 per $1,000 of actual value of taxable property ad valorem tax upon all taxable property within their jurisdiction for operations, maintenance, capital improvements and general Port purposes.

1991 REVENUE BOND DEBT SERVICE SCHEDULE

	Maturities Due	Interest	Total Debt Service
2000	$ 390,000	$ 1,422,250	$ 1,812,250
2001	410,000	1,397,680	1,807,680
2002	445,000	1,371,440	1,816,440
2003	475,000	1,342,515	1,817,515
2004	525,000	1,311,165	1,836,165
2005	2,225,000	1,275,990	3,500,990
2006	5,130,000	1,125,803	6,255,803
2007	5,475,000	776,963	6,251,963
2008	5,825,000	401,925	6,226,925
Total	**$20,900,000**	**$10,425,731**	**$31,325,731**

1992 REVENUE BOND DEBT SERVICE SCHEDULE

	Maturities Due	Interest	Total Debt Service
2000	$ 3,215,000	$ 1,085,115	$ 4,300,115
2001	3,385,000	921,150	4,306,150
2002	3,555,000	745,130	4,300,130
2003	3,740,000	556,715	4,296,715
2004	3,925,000	354,755	4,279,755
2005	2,480,000	138,880	2,618,880
Total	**$20,300,000**	**$ 3,801,745**	**$24,101,745**

1997 REVENUE BOND DEBT SERVICE SCHEDULE

	Maturities Due	Interest	Total Debt Service
2000	$ 1,225,000	$ 1,779,700	$ 3,004,700
2001	1,290,000	1,718,450	3,008,450
2002	1,350,000	1,653,950	3,003,950
2003	1,420,000	1,586,450	3,006,450
2004	1,485,000	1,521,130	3,006,130
2005	1,555,000	1,451,335	3,006,335
2006	1,630,000	1,378,250	3,008,250
2007	1,720,000	1,288,600	3,008,600
2008	1,810,000	1,194,000	3,004,000
2009	1,905,000	1,103,500	3,008,500
2010	2,000,000	1,008,250	3,008,250
2011	2,100,000	906,250	3,006,250
2012	2,205,000	798,625	3,003,625
2013	2,320,000	683,965	3,003,965
2014	2,445,000	561,005	3,006,005
2015	2,575,000	431,420	3,006,420
2016	2,710,000	294,945	3,004,945
2017	2,855,000	151,315	3,006,315
Total	**$34,600,000**	**$19,511,140**	**$54,111,140**

GENERAL OBLIGATION BONDS OUTSTANDING

Date of Issue	Maturity	Amount Outstanding	Purpose of Issue
May 15, 1991	June 1, 2011	$1,530,000	Terminal improvements, equipment and refund bonds.
July 15, 1992	December 1, 2004	1,675,000	Refund 1974 and 1987 Bond Issues
December 15, 1994	December 15, 2009	7,910,000	Dredging Blair and Sitcum Waterways
October 1, 1997	December 1, 2017	42,640,000	Terminal Improvements, Refund Bonds, and ULID

OTHER PORT DEBT OUTSTANDING

General Description	Amount Outstanding	Interest Rate
Real Estate Contracts	794,242	8.0%

TAX COLLECTION INFORMATION

	Amount of Tax Levy	Tax Collected as of 12/31/99	% Collected
1999	$6,548,188	$6,246,939	95.40%
1998	6,281,499	6,184,640	98.46%
1997	5,898,577	5,857,068	99.30%
1996	5,897,345	5,891,781	99.91%
1995	6,098,353	6,096,848	99.98%

PORT TAXING DISTRICT ASSESSED VALUATION

2000	$37,932,381,976
1999	35,244,911,558
1998	33,743,693,542
1997	31,703,559,198
1996	28,113,331,222

PROPERTY TAX LEVY AVAILABLE FOR CAPITAL IMPROVEMENT

	1999	**1998**	**1997**	**1996**	**1995**
Total Levy	$6,551,043	$6,290,378	$5,831,049	$5,906,348	$6,103,200
Less Designation for					
G. O. Debt Service	752,256	4,973,941	6,689,253	7,045,365	6,691,826
Subtotal	**1,798,787**	**1,316,437**	**(858,204)**	**(1,139,017)**	**(588,626)**
Supplements, Cancellations–Net	(2,855)	(8,879)	67,528	(9,002)	(4,847)
Refunds–Regular	(6,796)	(11,684)	(5,324)	7,238	6,209
Subtotal	**(9,651)**	**(20,563)**	**62,204**	**(1,764)**	**1,362**
Levy Available for Capital Improvement	**$1,789,136**	**$ 1,295,874**	**$ --**	**$ --**	**$ --**

CURRENT BOND RATINGS

	Revenue Bonds	General Obligation Bonds
Moody's Investor Services	A1	A1
Standard and Poor's Corporation	A+	A+

Port of Tacoma Regional Offices

Northwest
Denny Dalton
Jack Woods
Patti King
P.O. Box 1837
Tacoma, WA 98401
Telephone: (253) 383-5841
Seattle: (253) 838-0142
Fax: (253) 593-4534
Web site: www.portoftacoma.com
E-mail: dennyd@portoftacoma.com
jackw@portoftacoma.com
pking@portoftacoma.com

East Coast
Kevin Murphy
Port of Tacoma
Executive Suite at the Park
900 South Avenue
Staten Island, NY 10313
Telephone: (718) 816-7880
Fax: (718) 816-7813
E-mail: Kevin_c_murphy@classic.msn.com

Japan
Akira Tatara
Suite 505, Clear Akasaka
13-12, Akasaka 6 chome
Minato-ku, Tokyo 107-0052, Japan
Telephone: (011-813) 3588-8241
Fax: (011-813) 3588-8242
E-mail: potjpn@bg.mbn.or.jp

Singapore
Keith Hillier
Port of Tacoma Representative
Freight Links Express Districentre #06-01
9 Changi South St. 3
Singapore 486361
Telephone: (011-65) 255-2038
Fax: (011-65) 254-7251
E-mail: k_hillier@pacific.net.sg

Korea
Man-Lip Choy
Korean Microsystems, Inc.
#449-2 Jakjeon-Dong,
Buk-Ku, Inchon, Korea
Telephone: (011-82-32) 528-0411
Fax: (011-82-32) 524-2944
E-mail: isdn0780@soback.kornet.nm.kr

Hong Kong
Bill H. Y. Wong
Kristian Jebsens Limited
15th Floor, Qualipak Tower
122 Connaught Road West,
Hong Kong
Telephone: (011-852) 2861-0068
Fax: (011-852) 2520-6785
Cable: KRISJEB
E-mail: krisjeb@netvigator.com

Russian Far East Cooperative Trade Office
Olga V. Romanjuk, Director
7th Floor, 3b Strelnikova Street,
Vladivostok, Primorski Krai,
Russia 690060
Telephone: (011-7) 4232-497-335
Fax: (011-7) 4232-497-314
E-mail: washoff@online.ru

The Annual Report is the spring edition of *Pacific Gateway* Magazine, published quarterly by the Port of Tacoma.

Mick Shultz
Senior Editor

Bruce Sherman
Editor

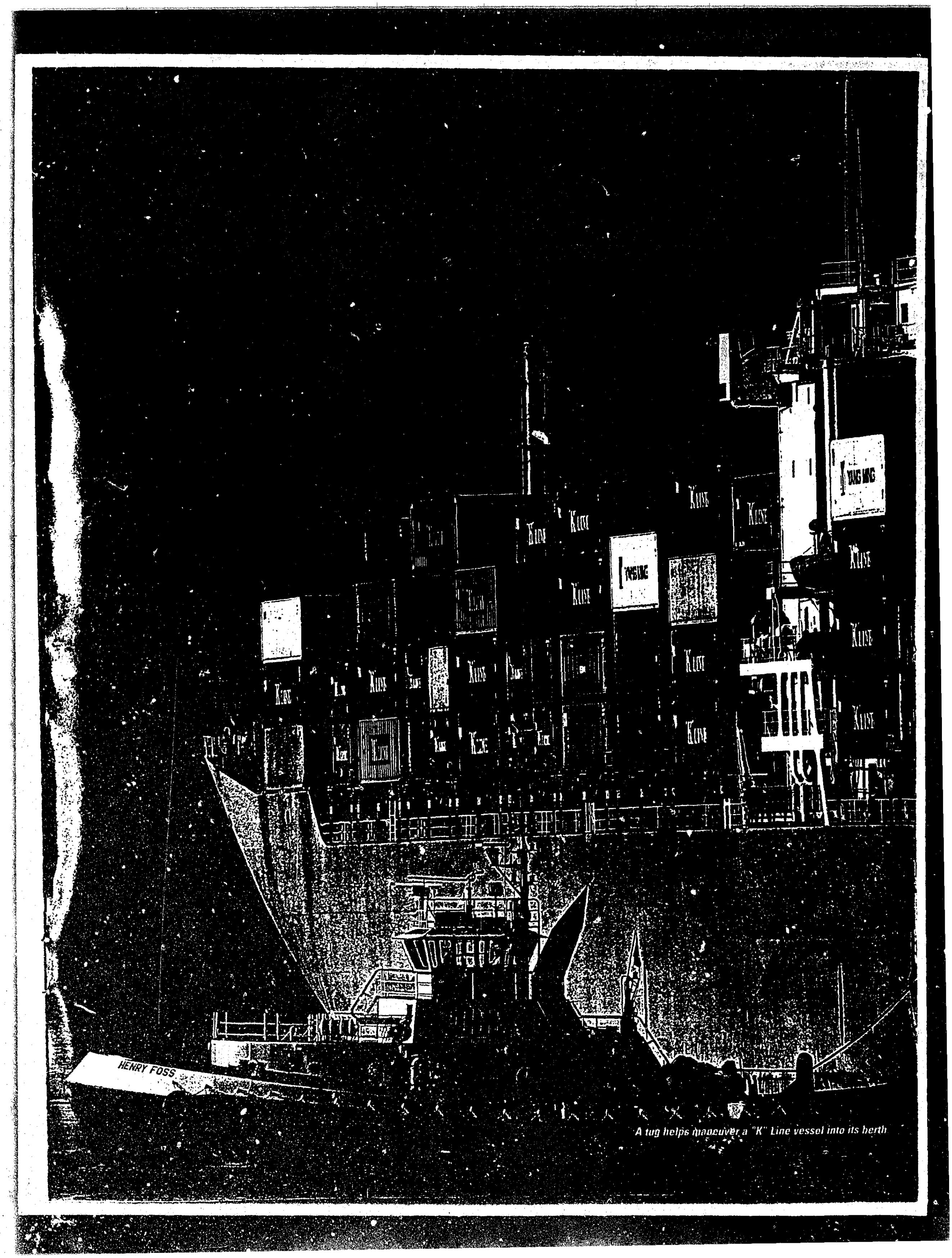
Scott Hamilton
Designer

Brian DalBalcon
Photographer

Port of Tacoma
P.O. Box 1837
Tacoma, WA 98401-1847
Telephone: (253) 383-5841
Seattle: (253) 838-0142
Fax: (253) 593-4534
Web site: www.portoftacoma.com

11M-4/2000

Printed on Recycled Paper



A tug helps maneuver a "K" Line vessel into its berth

PORT of
TACOMA
U.S.A.***

ATTACHMENT No. 3

(Port of Everett Annual Report)

1998 Business Recap
Executive Director John M. Mohr

The Port of Everett, as a municipal corporation, sets fees and collects revenues from Port tenants and users of Port services as well as taxes from property owners within the Port district. Profits derived from revenues are used to improve and upgrade our diverse facilities. The Port is governed by a three member commission whose members are elected from the Everett Port district which includes the City of Everett and part of Mukilteo. Commissioners serve six-year staggered terms and are responsible for setting Port policy, approving the budget and authorizing major capital expenditures. The Port directly employs 65-70 people who have a wide range of responsibilities including administration, maintenance, mechanical, and security. There are also numerous indirect employees working for tenants and users of Port facilities.

The Port has three major lines of business: the Marine Terminals where ships and barges carry cargo to and from points all over the world, Property Development which include properties in and around the marina and the old Weyerhaeuser Mill B site which is now called Riverside Business Park, and the Marina which provides moorage for over 2,000 commercial and pleasure craft.

Executive Director John Mohr has stated that 1998 proved to be not a great year for the Port of Everett, but a good year nonetheless. All three of the Port's business lines – Marine Terminals, Property Management and Marina turned in good solid performances. It was also a good year in that there were a number of beginnings at the Port of Everett. It was also a very good year in that the Port has positioned itself to continue to grow and develop well into the next millenium.

Marine Terminals

Marine Terminals continued to show growth in its container operations. This was offset somewhat by reductions in other general cargo activities, primarily centered around food products going into Russia. A bright spot in Port activities has been the leveling off of log exports which had declined in each of the six prior years. This is in sharp contrast to other Puget Sound Ports, which have continued to experience steep declines in log exports.

1998 also marked the completion of the Port's new 10-acre Pacific Terminal. The new dock facility is designed to be a multi-purpose facility capable of handling steel and containers, among other things. The facility is wired to handle up to 150 reefer containers, in addition to 1,000 non-refrigerated teu's. The new Pacific Terminal has a draft of –40 feet at dockside and is built is for heavy lift capability.

Property Management and Development

The most exciting activity in property development is the acquisition of 174 acres from the Weyerhaeuser Company. The Port acquired the recently cleaned-up brownfield site from the Weyerhaeuser Company in March of 1998 at a cost in excess of $12 million. The new Port of Everett industrial park, known as the Riverside Business Park, is adjacent to the Burlington

Northern-Santa Fe Delta Switchyard Facility, has excellent access to Interstate 5 and Highway 529 and is served by a new industrial capacity access bridge. The facility has been planned and is being permitted through the work of the Trammell Crow Company, nationally known developers of commercial property. When built out, the Riverside Industrial Park will have in excess of 1.3 million sq. ft. under roof, all designed to meet the needs of light industry and warehousing. The marketing focus will be toward companies that have marine industrial requirements, such as steel fabricators or auto importers. Site development is currently underway and the facilities are expected to be available for lease in the year 2000.

Marina

The Port of Everett operates the Pacific Northwest's largest marina. It has in excess of 2100 marina slips, in addition to significant side tying guest moorage facilities. The Port of Everett continues to add amenities to the finest marina in the Pacific Northwest. This year the Port built and opened yet another restroom and laundry facility. This one is to service the needs of the Port's North Marina patrons, as well as the users of the Port's visitor float.

This year the Port Commission directed Port staff to begin planning for the next phase of Marina development and expansion. In 1999 the Port Commission will designate a consultant to do the comprehensive planning for the Port's North Marina, as well as the development of the Baywood industrial property. Baywood is a former log yard site that has been cleaned up and filled with clean river sand. The site will be utilized as an alternative location for industrial facilities currently located at the North Marina. Once relocation has taken place, the Port can add significantly to the existing moorage through a planned expansion of the Port of Everett Marina. Currently the Port has a waiting list in excess of 800 vessels, most of which the Port should be able to accommodate in a newly expanded facility.

Mukilteo Tank Farm

The Port of Everett is taking a leadership position in the greater Mukilteo/Everett community to acquire the now abandoned U.S. Air Force fueling facility located adjacent to the Mukilteo Ferry Terminal. The Port is working with the City of Mukilteo, City of Everett, the Washington State Department of Transportation, Ferry system, and Sound Transit (formerly known as the Regional Transit Authority).

The Port has the superior position in the Federal surplus property disposal ranking for governmental agencies within Washington State. The Port intends to acquire the tank farm property and then finalize a comprehensive plan with its partners. Plans that have been discussed for the site include a new marina facility of 300-700 slips; a new ferry terminal for the Mukilteo-Clinton Ferry; a possible commuter rail facility for Sound Transit, plus significant public space and the potential for commercial development and other amenities.

Financial Results

Total Port Operating Revenues were 0.7% below 1997, but 2.0% ahead of budget, while total Port Operating Expenses were favorable by 1.6%, running below 1997. This produced Net Operating Income of $2.5 million, which was 3% better than the prior year. Nonoperating Revenues and Expenses were lower than 1997 by $435,000 due to declining interest earnings, as investments have been used to fund capital projects. The Net Income for the Port thus was $5.5 million in 1998, which was a 6% decrease from 1997.

The Port's property tax levy in 1998 was $.419 per $1,000 in assessed value for properties within the Port District, and those properties have an assessed value of $7.86 billion. In 1998 the Port's tax receipts were approximately $3 million.

Summary

The Port of Everett continues to have modest growth. It is expected that in the coming years the Port will continue to build out its facilities at the Marine Terminal, adding additional cargo handling equipment and capability. We fully anticipate that Marine Terminal growth, while moderating somewhat, will continue to grow and expand in the future and the Port will be able to continue its 3-5% historic growth rate well into the next millenium.

On the industrial property side, the Port looks forward to the build out of the Weyerhaeuser property, adding significantly to overall employment, while diversifying the economic base of the community. The Port also intends to develop significant additional marina spaces to meet the ever expanding interest in sailing and power boating in Puget Sound.

Independent Auditor's Report on Financial Statements

January 1, 1998 through December 31, 1998

COMPARATIVE BALANCE SHEET

December 31, 1998 and 1997

	1998	1997
ASSETS		
CURRENT ASSETS:		
Cash and Cash Equivalents (Note 1)	$ 473,830	$ 1,004,518
Investments (Note 2)	18,483,465	27,106,174
Taxes Receivable (Note 3)	96,521	78,735
Accounts Receivable (net of allowance for uncollectibles)	1,118,627	1,544,180
Interest Receivable	131,222	121,774
Inventory	32,931	37,416
Prepaid Expenses	161,134	174,445
Total Current Assets	20,497,731	30,067,242
RESTRICTED ASSETS: (Note 1)		
Cash and Cash Equivalents	3,585	2,164
Investments	6,659,297	2,838,098
Total Restricted Assets	6,662,882	2,840,262
CAPITAL ASSETS:		
Property, Plant and Equipment (Note 4)	170,076,151	154,252,449
Construction in Progress (Note 5)	876,205	1,025,720
Less: Accumulated Depreciation	(30,212,482)	(26,784,201)
Total Net Capital Assets	140,739,875	128,493,968
OTHER NONCURRENT ASSETS:		
Intangible Assets, net (Note 1)	4,255,905	4,040,073
Other Debits	477,008	307,933
Total Other Noncurrent Assets	4,732,912	4,348,006
TOTAL ASSETS	$ 172,633,400	$ 165,749,478
LIABILITIES AND EQUITY		
CURRENT LIABILITIES:		
Warrants Payable	$ 142,093	$ 330,491
Accounts Payable	594,391	1,188,695
Accrued Taxes Payable	143,367	108,443
Accrued Interest Payable	169,880	149,717
Current Portion of Long-term Obligations (Note 8)	2,415,000	2,065,000
Other Current Liabilities	171,811	145,774
Total Current Liabilities	3,636,542	3,988,121
LONG-TERM LIABILITIES:		
General Obligation Bonds, net (Note 8)	8,989,005	9,315,616
Revenue Bonds, net (Note 8)	16,013,553	14,437,128
Employee Leave Benefits	402,863	371,731
Total Long-term Liabilities	25,405,421	24,124,475
Total Liabilities	29,041,963	28,112,597
EQUITY:		
Contributed Capital (Note 10)	7,204,899	6,729,597
Retained Earnings	136,386,538	130,907,284
Total Equity	143,591,438	137,636,881
TOTAL LIABILITIES AND EQUITY	$ 172,633,400	$ 165,749,478

The notes to the financial statements are an integral part of this statement.

COMPARATIVE STATEMENT OF REVENUES, EXPENSES and CHANGES IN FUND EQUITY
For the Years Ended December 31, 1998 and 1997

	1998	1997
OPERATING REVENUES:		
Marina Operations	$ 4,716,442	$ 4,752,546
Marine Terminal Operations	6,295,461	6,672,711
Property Lease/Rental Operations	2,365,231	2,056,987
Total Operating Revenues	13,377,134	13,482,245
OPERATING EXPENSES:		
General Operations	4,018,017	4,561,497
Maintenance	2,107,863	2,073,700
General and Administrative	1,257,048	1,251,626
Depreciation (Note 4)	3,539,277	3,211,054
Total Operating Expenses	10,922,205	11,097,876
Operating Income	2,454,929	2,384,368
NONOPERATING REVENUES / (EXPENSES):		
Interest Income	1,334,872	1,800,310
Tax Receipts	3,043,676	3,023,089
Gain / (Loss) on Disposition of Assets	(5,595)	300
Interest Expense	(1,296,121)	(1,281,043)
Election Expense		(14,439)
Other Nonoperating Revenues / (Expenses)	(52,508)	(68,324)
Total Nonoperating Revenues / (Expenses)	3,024,325	3,459,892
NET INCOME	5,479,254	5,844,260
FUND EQUITY		
Fund Equity - January 1	137,636,882	131,556,161
Additions to Contributed Capital	475,302	236,460
Fund Equity - December 31	$ 143,591,438	$ 137,636,882

The notes to the financial statements are an integral part of this statement.

STATEMENT OF CASH FLOWS

For the Years Ended December 31, 1998 and 1997

	1998	1997
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Operating Income/(Loss)	$ 2,454,929	$ 2,384,368
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	3,539,277	
Change in Assets and Liabilities		
(Increase)/Decrease in accounts receivable	425,553	[illegible]
(Increase)/Decrease in inventory	4,484	([illegible]44)
(Increase)/Decrease in prepayments	13,311	14,779
Increase/(Decrease) in customer deposits	26,037	10,683
Increase/(Decrease) in accounts payable	(594,304)	(397,353)
Increase/(Decrease) in warrants payable	(188,398)	230,751
Increase/(Decrease) in taxes accrued	34,924	108,443
Increase/(Decrease) in employee benefits payable	31,132	21,178
Disposal of Assets	(5,595)	300
Net Cash Provided by Operating Activities	5,741,350	4,999,910
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Operating property taxes received	2,995,888	2,957,985
Miscellaneous taxes received	30,003	43,440
Non-operating receipts	15,033	563
Non-operating expenses		(14,439)
Net Cash Provided by Nonoperating Financing Activities	3,040,923	2,987,549
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Issuance of Bonds, net	3,650,354	
Acquisition and construction of capital assets	(16,001,015)	(12,309,466)
Principal paid on bonds	(2,065,000)	(2,005,000)
Interest paid on bonds	(1,275,959)	(1,295,020)
Bond issue expense	(233,998)	
Contributed Capital	475,302	236,460
Net Cash Used for Capital and Related Financing Activities	(15,450,316)	(15,373,027)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net purchase/sale of investment securities	4,801,511	6,386,117
Interest and dividends on investments	1,337,267	1,750,460
Escrow Accounts		39,319
Net Cash Provided by Investing Activities	6,138,777	8,175,897
Net Increase/(Decrease) in Cash and Cash Equivalents	(529,266)	790,329
Cash and Cash Equivalents at Beginning of Year	1,006,681	216,353
Cash and Cash Equivalents at End of Year	$ 477,416	$ 1,006,682

The notes to the financial statements are an integral part of this statement.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

The Port of Everett (the Port) was incorporated in 1918 and operates under the laws of the state of Washington applicable to a port district, as a municipal corporation under the provisions of Chapter 53 RCW. The Port is centrally located on Puget Sound at Port Gardner Bay about 125 miles inland from the Pacific Ocean. The boundaries of the Port District follow a line from Possession Sound extending eastward through the middle of Paine Field, north to the Snohomish River, and the line then follows Ebey Slough to Port Gardner Bay north of the City of Everett. It encompasses the greater city of Everett and the northern half of Mukilteo. The Port is situated on deep water Port Gardner Bay and next to Naval Station Everett. The accounting policies of the Port conform to generally accepted accounting principles for local governments. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following summary of the significant accounting policies is presented to assist the reader in interpreting the financial statements. The more significant policies are described below.

A. Reporting Entity

The Port is a special purpose government, independent of Snohomish County and City of Everett government, and provides marine terminal, marina, and property lease/rental operations to the general public and is supported primarily through user charges.

The Port is governed by a three member Board of Commissioners, elected by Port district voters. As policy makers, they delegate certain administrative authority to the Executive Director to conduct operations of the Port. As required by generally accepted accounting principals, management has considered all potential component units in defining the reporting entity. These financial statements present the Port and its component unit. The component unit discussed below is included in the Port's reporting entity because of the significance of its operational or financial relationship with the Port.

The Industrial Development Corporation of the Port of Everett, a public corporation, is authorized to facilitate the issuance of tax-exempt nonrecourse revenue bonds to finance industrial development within the corporate boundaries of the Port. Revenue bonds issued by the Corporation are payable from revenues derived as a result of the industrial development facilities funded by the revenue bonds. The bonds are not a liability or contingent liability of the Port or a lien on any of its properties or revenues other than industrial facilities for which they were issued. The Port's Board of Commissioners governs the Industrial Development Corporation. The Industrial Development Corporation's account balances and transactions are included as a blended unit within the Port's financial statements.

The Ports financial resources are provided by marine terminal facilities which handle forest and agricultural products, alumina, aircraft parts, and various other commodities; a marina providing moorage for 2,050 pleasure and fishing vessels; and property lease/rentals providing more than 80 property leases.

B. Basis of Accounting and Presentation

The accounting records of the Port of Everett are maintained in accordance with methods prescribed by the State Auditor under authority of Chapter 43.09 RCW. The Port uses the *Budgeting, Accounting and Reporting System for Proprietary-Type Districts* in the State of Washington.

Funds are accounted for on a cost of services or "capital maintenance" measurement focus. This means that all assets and all liabilities (whether current or noncurrent) associated with their activity are included on their balance sheets. Their reported fund equity (net total assets) is segregated into contributed capital and retained earnings components. Operating statements present increases (revenues and gains) and decreases (expenses and losses) in net total assets. The Port discloses changes in cash flows by a separate statement that presents the operating, investing and financing activities.
The Port uses the full-accrual basis of accounting where revenues are recognized when earned and expenses recognized when incurred. Fixed asset purchases are capitalized and depreciated over their useful life, and long-term liabilities are accounted for in the appropriate fund.

The Port has elected under GASB Statement 20 to not follow FASB statements issued after November

20, 1989. In accordance with GASB statement 32, the Port is not including information on deposits for Deferred Compensation in this year's statement. In addition, the information presented in the previous year's statements has been removed.

C. Assets, Liabilities and Equities

1. Cash and Cash Equivalents

   It is the Port's policy to invest all temporary cash surpluses. At December 31, 1998, cash and cash equivalents totaled $477,415. This amount is classified on the balance sheet as cash and cash equivalents. The amounts reported as cash and cash equivalents also include compensating balances maintained with certain banks in lieu of payments for services rendered. The average compensating balances maintained during 1998 were approximately $100,000.

   For purposes of the Statement of Cash Flows the port considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

2. Investments

   As of December 31, 1998, investments totaled $25,142,762 of which $6,659,297 was restricted for specific uses. See Note 2.

3. Receivables

   Taxes receivable consists of property taxes and related interest and penalties (See Note 3). Accrued interest receivable consists of amounts earned on investments at the end of the year. Accounts receivable consists of amounts due from individuals or organizations for services provided. Receivables have been recorded net of estimated uncollectible amounts. Because property taxes are considered liens on property, no estimated uncollectible amounts are established. Estimated uncollectible amounts for other receivables are $30,000.

4. Inventories

   Inventories are valued by the weighted average method, which approximates year-end cost.

5. Restricted Assets

   In accordance with bond resolutions and certain agreements, separate restricted accounts are required to be established. These accounts contain resources for construction and funds for specified uses. At December 31, 1998 the restricted assets totaled $6,662,882.

6. Fixed Assets and Depreciation

   Fixed assets are acquisitions of significant value (greater than $1,000) and having a useful life extending beyond two years. These are recorded at cost. Fixed assets acquired with contributed funds are also capitalized (See Note 4).

7. Intangible Assets

   As part of the sale of property to the Department of Defense for the Navy Homeport, the Port was required to assist in mitigation of traffic impacts. As part of the mitigation effort the Port contributed to the construction of the Alverson Street bridge. The Port has no ownership interest in this bridge. This asset will be amortized over a 50 year life.

8. Employee Leave Benefits

   Employee leave benefits are accrued leave payable to employees of the Port. Vacation pay, which may be accumulated up to 48 days, is payable upon resignation, retirement or death. Sick leave may accumulate up to 180 days. Upon separation without cause, employees are paid for accumulated sick leave at 50% of their final balance but not more than 90 days (50% of 180 days). The Port accrues vacation and sick leave benefits as earned. At December 31, 1997 and 1998 the recorded liability for unpaid vacation and sick leave was $371,731 and $402,863 respectively.

9. Unamortized Debt Expense

   Costs relating to the sale of bonds are deferred and amortized over the lives of the various bond issues.

NOTE 2 - DEPOSITS AND INVESTMENTS

As required by state law, all deposits and investments of the Port's funds are obligations of the US Government, the State Treasurer's Investment Pool or certificates of deposit with Washington state banks and savings and loan institutions.

The Port's deposits and certificates of deposit are entirely covered by federal deposit insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

The Port used quoted market price to estimate the fair value of its investments.

The Port's investments are categorized to give an indication of the risk assumed at year end. The following summary shows the Port's investments at year end categorized by risk. Category 1 includes investments that are insured, registered or held by the Port or its agent in the Port's name.

	Category 1 Par Amount	Fair Value
Certificates of Deposit	$3,318,870	3,318,870
US Government Securities	1,867,705	1,844,522
Sub-Total	5,186,575	5,163,392
State Treasurer's Investment Pool		19,979,370
Total		$25,142,762

NOTE 3 - PROPERTY TAXES

The County Treasurer acts as agent to collect property taxes levied in the county for all taxing authorities. The County Treasurer distributes collections after the end of each month to the Port. A revaluation of all property is required every four years.

<u>Property Tax Calendar</u>

January 1	Taxes are levied and become an enforceable lien against properties.
February 14	Tax bills are mailed.
April 30	First of two equal installment payments is due
May 31	Assessed value of property established for next years levy at 100% of market value.
October 31	Second installment is due.

Property taxes are recorded as a receivable when levied. During the year, property tax revenues are recognized in the month when the County Treasurer collects cash. No allowance for uncollectible taxes is established because delinquent taxes are considered fully collectible.

The Port may levy up to $.45 per $1,000 of assessed valuation for general government services. The rate is limited by the Washington State Constitution and Washington State law, RCW 84.55.010. The Port may also levy taxes at a lower rate.

The Port's regular levy for 1998 was $.419 per $1,000 on an assessed valuation of $7.217 billion for a total regular levy of $3,023,714. In 1997 the regular tax levy was $.419.

NOTE 4 - FIXED ASSETS AND DEPRECIATION

Major expenditures for fixed assets and major repairs that increase useful lives are capitalized. Maintenance, repairs, and minor renewals are accounted for as expenses when incurred. All fixed assets are valued at historical cost.

The Port has acquired certain assets with funding provided by federal and state financial assistance programs. Depending on the terms of the agreements involved, the government could retain an equity interest in these assets. However, the Port has sufficient legal interest to accomplish the purposes for which the assets were acquired and has included such assets within the applicable account.

Depreciation expense is charged to operations to allocate the cost of fixed assets over their estimated useful lives using the straight line method. Buildings and improvements are assigned lives of 20 to 50 years and equipment 5 to 25 years. Accumulated depreciation on assets at December 31, 1998 is as follows:

Buildings & Structures	$22,762,917
Improvements	4,260,486
Equipment	3,189,079
Total Accumulated Depreciation	$30,212,482

NOTE 5 - CONSTRUCTION IN PROGRESS

Construction in progress (CIP) represents expenditures related to projects authorized by the Commission in the 5 year CIP plan but which have not been completed.

	5 Year CIP Authorization as of December 31	Expended during 1998	CIP balances at December 31
Marine Terminal	$14,164,000	$2,072,693	$227,383
Properties & Real Estate	15,577,000	12,380,423	98,037
Transportation	1,660,000	350,777	91,384
Marina	5,537,500	999,583	412,759
Administration	105,000	151,533	46,641
Total	$37,043,500	$15,955,009	$876,204

NOTE 6 - PENSION PLANS

Substantially all of the Port's full-time and qualifying part-time employees participate in the Public Employees' Retirement System (PERS). This is a statewide local government retirement system administered by the Department of Retirement Systems, under cost-sharing multiple-employer defined benefit public employee retirement systems.

Historical trend information regarding each plan is presented in the State Department of Retirement Systems annual financial report. A copy of this report may be obtained at:

Department of Retirement Systems
Capital Plaza Building
PO Box 48380
Olympia, WA 98504-8380

A. Description of Plan

PERS is a cost-sharing defined benefit multiple-employer system. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts (other than judges); employees of legislative committees; college and university employees not in national higher education retirement programs; judges of district and municipal courts; noncertified employees of school districts; and employees of local government. PERS contains two "plans." Participants who joined the system by September 30, 1977, are Plan I members. Those joining thereafter are enrolled in Plan II. Retirement benefits are financed from employee and employer contributions and investment earnings. Retirement benefits in both Plan I and Plan II are vested after completion of five years of eligible service.

Plan I members are eligible for retirement after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2 percent of the final average salary per year of service, capped at 60 percent. If qualified, after reaching age 66 a cost-of-living allowance is granted based on years of service credit and is capped at 3 percent annually.

Plan II members may retire at the age of 65 with five years of service, or at 55 with 20 years of service, with an allowance of 2 percent per year of service of the final average salary. Plan II retirements prior to 65 are actuarially reduced. There is no cap on years of service credit and a cost of living allowance is granted, capped at 3 percent annually.

B. Funding Policy

Each biennium the state Pension Funding Council adopts Plan I employer contribution rates needed to fully amortize the total costs of the plan. Employee contribution rates for Plan I are established by statute at 6 percent and do not vary from year to year. The employer and employee contribution rates for Plan II are set by the director of the Department of Retirement Systems based on recommendations by the Office of the State Actuary to continue to fully fund the plan. All employers are required to contribute at the level established by state law. The methods used to determine the contribution rates are established under state statute in accordance with Chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current year covered payroll, as of December 31, 1998, were:

	Plan I Required	Plan II Required
Employer*	7.32%	7.32%
Employee	6.00%	4.65%

*The employer rates do not include the employer administrative expense fee currently set at 0.18%

The Port's required contributions for the years ended December 31, were:

	Plan I Required	Plan II Required
1998	$60,106	$152,518
1997	62,688	139,533
1996	65,863	128,081

NOTE 7 - CONTINGENT LIABILITIES AND LITIGATION

The Port has recorded in its financial statements all material liabilities, including an estimate for situations which are not yet resolved but where, based on available information, management believes it is probable that the Port will have to make payment. In the opinion of management, the Port's insurance policies are adequate to pay all known or pending claims.

The Port is contingently liable for repayment of refunded debt which is discussed in Note 8.

In addition, the Port participates in federal and state assisted programs. These grants are subject to audit by the grantors or their representatives. Such audits could result in requests for reimbursement to the grantor agencies for expenses disallowed under the terms of the grants. The Port's management believe that such disallowance, if any, is not material.

NOTE 8 - LONG-TERM DEBT

The Port issues general obligation and revenue bonds to finance acquisition, purchase or construction of various projects. The Port has also issued bonds to refund previously issued debt. See the following table for a listing of the outstanding debt of the Port and the annual requirements to amortize it, including principal and interest.

Year	1996 Series A&B General Obligation Bonds Principal & Interest	1996 Series A&B Revenue Bonds Principal & Interest	1998 Series A&B Revenue Bonds Principal & Interest
1999	$824,692	$1,555,122	$1,292,161
2000	824,017	1,564,435	1,286,961
2001	827,630	1,570,822	1,290,561
2002	825,292	1,558,930	1,287,561
2003	827,052	1,553,117	1,293,161
2004-2016	10,751,797	1,582,080	6,107,207
Total	$14,880,480	$9,384,506	$12,557,612

Funds are transferred to the fiscal agent for redemption of principal and interest payments.

As of December 31, 1998, the trustee was holding cash and investments of $25,893 for the 1977 Revenue Bonds and $5,487 for the 1979 Revenue Bonds, which were refunded by the 1996 Revenue Bonds. Funds held by the trustee are expected to fund the 1977 and 1979 debt service fully.

Limitation of indebtedness is provided for in Chapter 39.36 RCW with unvoted General Obligation Bond debt limited to .25% of the assessed value of the taxable property in the port district.

At December 31, 1998, the port district's assessed value and limitation of unvoted General Obligation debt are as follows:

Total assessed value	$7,858,237,663
.25% limitation of indebtedness	19,645,594
Unvoted GO Bonds issued	9,380,000
Unvoted GO Bond margin	10,265,594

General Revenue Bond Coverage (Last Ten Fiscal Years)

Year	Gross Revenues	Direct Expenses	Avail. For Debt Service	Revenue Bonds	Coverage*
1988	$ 12,595,000	$ 4,001,262	$ 8,593,738	$ 2,929,667	2.93
1989	15,104,533	4,284,853	10,819,680	2,859,067	3.78
1990	16,555,341	5,030,523	11,524,818	2,713,143	4.25
1991	16,338,111	5,274,920	11,063,191	2,513,686	4.40
1992	15,070,980	6,223,180	8,847,800	2,385,003	3.71
1993	11,690,237	6,470,307	5,219,930	2,445,133	2.1[illegible]
1994	12,167,283	6,972,766	5,194,517	2,481,129	2.09
1995	12,300,947	6,409,247	5,891,700	2,513,053	2.34
1996	16,260,906	7,081,923	9,178,983	2,137,606	4.29
1997	18,306,506	7,864,291	10,442,215	2,457,428	4.25
1998	17,776,477	7,578,771	10,197,706	3,411,715	2.99

*The current bond coverage ratio requirement is 1.35

NOTE 9 - RISK MANAGEMENT

The Port maintains commercial insurance coverage against most normal hazards except for unemployment insurance where it has elected to become self-insured.

General liability coverage is in effect to a limit of $1 million with a $25,000 deductible. Excess liability coverage is in effect with a limit of $50 million over the first $1 million of loss.

Commercial property coverage with a loss limit of $105 million with a deductible of $25,000 is in effect. In addition, the Port maintains standard business automobile, construction, and boiler and machinery coverage.

In addition, the Port provides medical, vision, dental, life, and long-term disability insurance coverage through standard plans. The Port does not administer any of these plans.

NOTE 10 - CONTRIBUTED CAPITAL

Contributed capital consists of contributed fixed assets or contributions for fixed asset acquisition from other governments, customers, developers or other sources. Additions to Contributed Capital in 1998 consisted of $70,835 from federal sources, $300,423 from state/local sources, and $104,045 from private sources.

NOTE 11 - RELATED PARTIES

The Port has a lease with Scuttlebutt Brewing Co. LLC, a limited liability company (Scuttlebutt). One of the principals of Scuttlebutt is Phil Bannan, a port commissioner. The lease was entered into prior to Commissioner Bannan's election to the Port Commission. The lease is for a period of 5 years, with 3 renewal options of 5 years each. The monthly rental is $1,250 per month, with an annual adjustment based upon changes in the Consumer Price Index. As of December 31, 1998, Scuttlebutt was current on all payments to the Port.

NOTE 12 – MATERIAL CUSTOMERS

The Port has one customer which represents 22.9 % of the operating receipts for 1998. The total billings for 1998 equaled $3,059,790 and the port has a receivable from the company as of December 31, 1998 of $402,760.

NOTE 13 - SEGMENT INFORMATION

The Port operates shipping marine terminals, a marina, and leases industrial property, which are primarily financed by user charges. The key financial data for the year ended December 31, 1998 for these facilities are as follows:

	Marine Terminals	Marina	Property Leases	Total
Operating Revenue	6,295,461	4,716,442	2,365,231	13,377,134
Operating Expense	2,469,200	3,052,695	703,984	6,125,879
Depreciation Expense	2,203,742	746,056	358,248	3,308,046
Income From Operations	1,722,519	917,691	1,302,999	3,943,209
Administrative Expense				1,488,280
Net Operating Income				2,454,929
Non-Operating Revenues, net				3,024,325
Net Income				5,479,254

End of Footnotes

REQUIRED SUPPLEMENTARY INFORMATION

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely affect the Port's operations as early as fiscal year 1999.

The Port of Everett has completed an inventory of computer systems and other electronic equipment that may be affected by the year 2000 issue and that are necessary to conducting Port operations. Based on this inventory, the Port is in the remediation stage. The Port has entered into a contract with an outside vendor to replace the marina billing and management software with year 2000 complaint software. This contract was entered into as of December 9, 1998 for a total of $97,650, the cost of which will be shared with 5 other ports. Testing and validation of the software will be completed prior to acceptance of the software. The Port has received assurances from vendors that the remainder of the systems necessary for Port operations are year 2000 compliant.

Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determined until the year 2000 and thereafter. Management cannot assure that the Port is or will be year 2000 ready, that the Port's remediation efforts will be successful in whole or in part, or that parties with whom the Port does business will be year 2000 ready.

ATTACHMENT No. 4

(Sections 127 and 128 -- Canada Transportation Act of 1996)

(Regulations Respecting the Interswitching of Rail Traffic -- Canadian Transportation Agency)

Web Site: http://canada.justice.gc.ca/FTP/EN/Laws/Chap/C/index.html

Canada Transportation Act -- CHAPTER C-10.4 (1996, c. 10)
****
**
* File : C-10.4.TXT *
* Updated to : August 31, 1999 *
* *
* Note: This consolidation is not an official version of the law. Also, *
* because this file is text-only, it does not contain formatting or graphics. *
****
**

Canada Transportation Act

CHAPTER C-10.4 (1996, c. 10)

[C-10.4]

An Act to continue the National Transportation Agency as the Canadian Transportation Agency, to consolidate and revise the National Transportation Act, 1987 and the Railway Act and to amend or repeal other Acts as a consequence

[Assented to 29th May, 1996]

Her Majesty, by and with the advice and consent of the Senate and House of Commons of Canada, enacts as follows:

SHORT TITLE

Short title

1. This Act may be cited as the Canada Transportation Act.

HER MAJESTY

Binding on Her Majesty

2. This Act is binding on Her Majesty in right of Canada or a province.

APPLICATION

Application generally

3. This Act applies in respect of transportation matters under the legislative authority of Parliament.

Conflicts

4. (1) Subject to subsection (2), where there is a conflict between any order or regulation made under this Act in respect of a particular mode of transportation and any rule, order or regulation made under any other Act of Parliament in respect of that particular mode of transportation, the order or regulation made under this Act prevails.

Competition Act

(2) Nothing in or done under the authority of this Act affects the operation of the Competition Act.

NATIONAL TRANSPORTATION POLICY

Declaration

5. It is hereby declared that a safe, economic, efficient and adequate network of viable and effective transportation services accessible to persons with disabilities and that makes the best use of all available modes of transportation at the lowest total cost is essential to serve the transportation needs of shippers and travellers, including persons with disabilities, and to maintain the economic well-being and growth of Canada and its regions and that those objectives are most likely to be achieved when all carriers are able to compete, both within and among the various modes of transportation, under conditions ensuring that, having due regard to national policy, to the advantages of harmonized federal and provincial regulatory approaches and to legal and constitutional requirements,

(a) the national transportation system meets the highest practicable safety standards,

(b) competition and market forces are, whenever possible, the prime agents in providing viable and effective transportation services,

(c) economic regulation of carriers and modes of transportation occurs only in respect of those services and regions where regulation is necessary to serve the transportation needs of shippers and travellers and that such regulation will section 113.

No investigation or arbitration of confidential contracts

(2) No party to a confidential contract is entitled to submit a matter governed by the contract to the Agency for final offer arbitration under section 161, without the consent of all the parties to the contract.

Interswitching

Application to interswitch traffic between connecting lines

127. (1) If a railway line of one railway company connects with a railway line of another railway company, an application for an interswitching order may be made to the Agency by either company, by a municipal government or by any other interested person.

Order

(2) The Agency may order the railway companies to provide reasonable facilities for the convenient interswitching of traffic in both directions at an interchange between the lines of either railway and those of other railway companies connecting with them.

Interswitching limits

(3) If the point of origin or destination of a continuous movement of traffic is within a radius of 30 km, or a prescribed greater distance, of an interchange, a railway company shall not transfer the traffic at the interchange except in accordance with the regulations.

Extension of interswitching limits

(4) On the application of a person referred to in subsection (1), the Agency may deem a point of origin or destination of a movement of traffic in any particular case to be within 30 km, or a prescribed greater distance, of an interchange, if the Agency is of the opinion that, in the circumstances, the point of origin or destination is reasonably close to the interchange.

Regulations

128. (1) The Agency may make regulations

(a) prescribing terms and conditions governing the interswitching of traffic, other than terms and conditions relating to safety;

(b) determining the rate per car to be charged for interswitching traffic, or prescribing the manner of determining that rate, including the adjustments to be made to that rate as a result of changes in costs, and establishing distance zones for those purposes; and

(c) prescribing, for the purposes of subsections 127(3) and (4), a greater distance than 30 km from an interchange.

Cost savings to be considered

(2) In determining an interswitching rate, the Agency shall take into consideration any reduction in costs that, in the opinion of the Agency, results from moving a greater number of cars or from transferring several cars at the same time.

Limit on rate

(3) In determining an interswitching rate, the Agency shall consider the average variable costs of all movements of traffic that are subject to the rate and the rate must not be less than the variable costs of moving the traffic, as determined by the Agency.

Transfer of lines does not affect entitlement

(4) For greater certainty, the transfer of a railway line, or an operating interest in it, under Division V or section 158 of the National Transportation Act, 1987 does not affect any entitlement to an interswitching rate.

Review of interswitching regulations

(5) The Agency shall review the regulations when the circumstances warrant and at least once in every five year period after the regulations are made.

Competitive Line Rates

Application

129. (1) Sections 130 to 136 apply where

(a) a shipper has access to the lines of only one railway company at the point

|français|

REGULATIONS RESPECTING THE INTERSWITCHING OF RAIL TRAFFIC

SHORT TITLE

1. These Regulations may be cited as the *Railway Interswitching Regulations.*

INTERPRETATION

2. In these Regulations,

"Act" means the *National Transportation Act, 1987; (Loi)*

"car block" means 60 or more cars that, as a block, are interswitched at an interchange and are destined to, or originate from a single shipper at a siding; *(rame de wagon)*

"siding" means

(a) a private siding connecting with a line of railway of a terminal carrier,

(b) a team track of a terminal carrier,

(c) a track where traffic may be loaded or unloaded directly from or into a shipper's facility abutting a terminal carrier's tracks, and

(d) a track for loading or unloading in a public stockyard,

but does not include

(e) a track used by a terminal carrier for the transfer of traffic between cars or between a car and a warehouse owned by a terminal carrier, or

(f) a track serving a reload or distribution compound, a container terminal or any other facility operated by the terminal carrier or its agent or operated for the terminal carrier's own purposes; *(voie d'évitement)*

"terminal carrier" means a railway company that interswitches traffic at an interchange to or from a siding. *(transporteur de tête de ligne)*

APPLICATION

3. (1) These Regulations do not apply

(a) in respect of the operation of transferring traffic, where a terminal carrier has interswitched traffic to a siding for unloading in accordance with these Regulations and transfers the traffic to another siding at the request of a shipper or another railway company; and

(b) in respect of the operations and administration of a railway company, where in the immediately preceding three year period that company derived at least 90 per cent of its gross freight revenues from interswitching, according to the returns prepared by the company under section 344 of the *Railway Act*.

(2) Where the Agency determines that a railway company does not qualify for an exemption from the application of these Regulations under paragraph (1)(b) because the company derived less than 90 per cent of its gross freight revenues from interswitching in the immediately preceding three year period, these Regulations

(a) become applicable to the company 10 days after the day on which the Agency sends the company notification of that determination; and

(b) apply to the company for a period of one year after the day on which they became applicable to the company under paragraph (a).

(3) A railway company referred to in subsection (2) may, on the expiration of the period referred to in paragraph (2)(b), present to the Agency evidence that it qualifies for an exemption from the application of these Regulations under paragraph (l)(b).

(4) The Agency shall, within 60 days after receiving the evidence referred to in subsection (3), notify the company as to whether it qualifies for an exemption.

GENERAL

4. A terminal carrier shall at all times furnish to interswitched traffic a level of service equal to the level of service accorded the terminal carrier's line haul traffic.

5. A railway company for whom a terminal carrier interswitches a car shall deliver an empty car to the terminal carrier at the interchange for delivery to a siding for loading.

6. No charge shall be made by a terminal carrier for the delivery of an empty car from an interchange to a siding for loading or for the return of an empty car to an interchange after unloading.

INTERSWITCHING DISTANCE ZONES

7. (1) For the purposes of this section, the distance defining the outer limit of interswitching zone 1, 2 or 3 shall be measured along the line of track of the terminal carrier.

(2) For the purposes of these Regulations, the following interswitching distance zones are established:

(a) interswitching distance zone 1, being a zone that includes sidings located wholly or partly within 6.4 km of an interchange;

(b) interswitching distance zone 2, being a zone that includes sidings located

(i) wholly or partly within 10 km of an interchange, and

(ii) wholly outside interswitching distance zone 1;

(c) interswitching distance zone 3, being a zone that includes sidings located

(i) wholly or partly within 20 km of an interchange, and

(ii) wholly outside interswitching distance zones 1 and 2; and

(d) interswitching distance zone 4, being a zone that includes sidings located

(i) wholly or partly within a radius of 30 km of an interchange, and

(ii) wholly outside interswitching distance zones 1, 2 and 3.

INTERSWITCHING RATES

8. Subject to section 9, the interswitching rate charged in any year by a terminal carrier for traffic originating in or destined to an interswitching distance zone shall not exceed the interswitching rate precribed for that zone in the table for that year set out in the schedule.

9. Where a siding is located wholly or partly within the interswitching distance zone 4 and the point of connection with the siding is more than 40 km from an interchange along the line of track of a terminal carrier, the interswitching rate for each car is increased for each kilometre over 40 km by an amount equal to the rate per kilometre set out in column IV or V, as the case may be, of item 4 of the schedule.

INTERSWITCHING RATES FOR THE PURPOSE OF CALCULATING COMPETITIVE LINE RATES

10. For the purpose of subsection 137(1) of the Act, the rate referred to in paragraph (a) of that subsection is the rate determined in accordance with section 8 for interswitching distance zone 4 and the rate is applicable for the first 25 miles of the movement of traffic along the line of track.

SCHEDULE

(Sections 8 to 10)

INTERSWITCHING RATES

Item	Column I Interswitching distance zone	Column II Rate per car for interswitching traffic to or from a siding ($)	Column III Rate per car for interswitching a car block ($)	Column IV Additional rate per kilometre for interswitching a car ($)	C A pe in ca bl ($
1.	Zone 1	210	65	N/A	
2.	Zone 2	230	70	N/A	
3.	Zone 3	275	90	N/A	
4.	Zone 4	365	105	4.20	

Note: Amendments to section 9 and the schedule of interswitching rates came into effect on November 20, 1997.

For further information, contact Michel Maisonneuve (819) 953-2255.

Return to Table of Contents